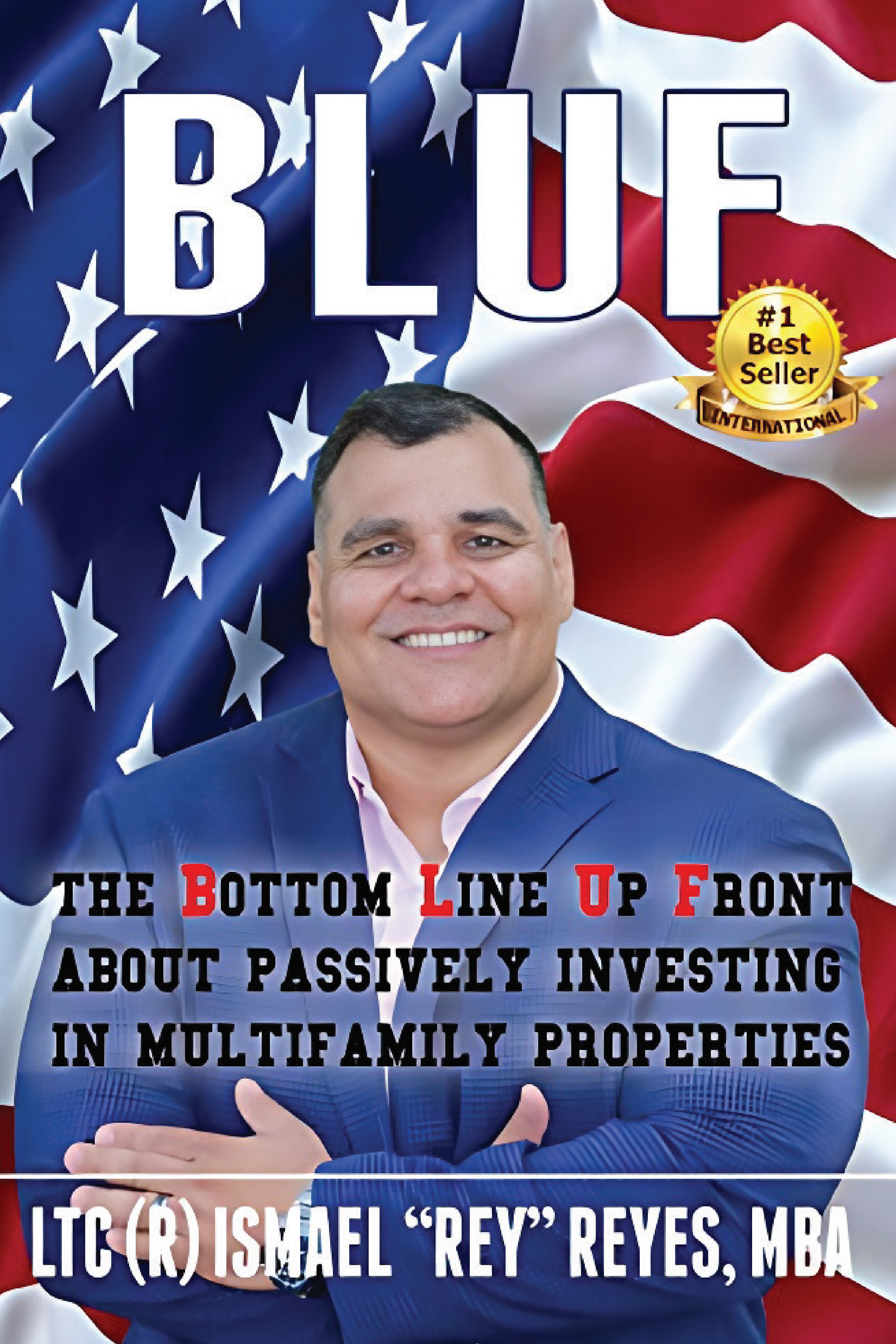
BLUF



THE BOTTOM LINE UP FRONT ABOUT PASSIVELY INVESTING IN MULTIFAMILY PROPERTIES

LTC (R) ISMAEL "REY" REYES, MBA

BLUF

The Bottom Line Up Front about Passively Investing in Multi-family Properties

Written By

LTC (R) Ismael "Rey" Reyes, MBA

Disclaimer

The purpose of this book is to familiarize you with syndication deals; syndication deals in real estate as an option for investments that might not have been on your radar or seemed impossible before. My hope is that reading this book will inform you about syndication deals and open a whole new world of investment opportunities to you, as it has for me in my life.

Although I'm going to be showing you some of the ins and outs of syndication deals, I'm not a real estate attorney or tax professional. I do not intend for this book to be a legal guideline or to replace expert advice from real estate and business attorneys and tax professionals. Seek your own legal advice and counsel before investing.

Acknowledgments

I want to thank my lovely wife and business partner, Mayerlyn Reyes. From the day we met over 22+ years ago to today, you have been my rock, encouraging me when I needed it, sacrificing during all our military moves, my deployments and temporary travel so that I could do my duty; and now, supporting me so I can do what I love, what gives me purpose.

I'd like to also thank my two sons, Ismael and Gabriel Reyes, who bore the burden of being Army brats (yes, this is a term of endearment) through just about their entire childhood. They were also with my wife and I when we toured properties, during several rehab or make-ready projects, and helped me edit this book.

Table of Contents

Foreword ... **vii**

Introduction ... **xi**

Chapter 1: What Is Syndication? ... **1**
- Defining a Syndication ... 2
- Typical Legal Structure for Syndications ... 3
- Why Consider a Syndication? ... 7

Chapter 2: Key Team Members in a Syndication ... **9**
- Sponsor ... 9
- Investors ... 12
- Other Key Members in a Syndication ... 15

Chapter 3: Tax Advantages of Multi-family Properties ... **21**
- Tax Advantages that Apply for Multi-family Properties ... 21
- Tax Implications from Syndication Structuring ... 25

Chapter 4: Why Multi-family Over Single-family? ... **29**
- Differentiating Multi-family and Single-family Units ... 29
- Why Choose Multi-family? ... 31

Chapter 5: Why Multi-family Over CRE? ... **37**
- Multi-family as a Part of CRE ... 37
- Why Choose Multi-family Properties? ... 39

Chapter 6: Key Terminology ... **45**
- Key Real Estate Investments Terms ... 45
- Internal Rate of Return (IRR) ... 48
- Multi-family Real Estate Terms ... 48

Chapter 7: Determining Investment Criteria ... **53**
- Neighborhood & Surroundings ... 56
- Examining the Macro Environment ... 59
- Pro-Business Climate ... 61
- Property Quality ... 63

Financials 64
Evaluating a Property 66

Chapter 8: Define & Vet the Sponsor 69

Chapter 9: Define & Vet the Investment Team 81

Who Is the Team? 81

Chapter 10: Analyzing the Deal 89

Financial Structures 89
Partner Roles 92
Market Comparison 93
Liabilities 95
Assets 96
Project Plan 97

Chapter 11: What Are Operating Agreements & PPMs? 99

Operating Agreement 99
Private Placement Memorandum (PPM) 103
Legal Consultations 105

Chapter 12: Property Purchased, Now What? 107

Multi-family Post-Purchase Responsibilities 107
Asset Management 109
Selling the Property 111
Wrapping Up the Deal 111

Summary 113

About Ismael "Rey" Reyes 115

Foreword

My name is Michael Blank. I'm an entrepreneur, investor, and investment coach. My passion is teaching people of all kinds how to achieve financial freedom in 3-5 years through investing in multi-family apartment properties. I've been investing in real estate for more than a decade, even though I started my career doing software development. It's a fundamental belief of mine that anyone can find financial freedom in real estate, no matter what your background is.

I first met Ismael "Rey" Reyes at a real estate investment conference that we both attended in DC. Although it was my first time meeting him in person, we had already been working together and connecting online through my Real Estate Syndication program. He signed up to use my Syndicated Deal Analyzer to underwrite his own multi-family projects so he could jump into multi-family investing for himself.

From the beginning, Rey stood out as someone dedicated to making this investment avenue work for him.

As he started using the deal analyzer successfully on his own investments, I asked him to act as an advisor on a Mastermind Slack channel for aspiring and existing real estate investors. He's still doing that today, helping to teach people about getting into multi-family property investing.

We've been working together for a while now in one way or another. I wouldn't ever want to put words in his mouth, but I believe we met at a crucial time, with my program helping to launch Rey forward and give him the confidence to go out and join his first multi-family property deal.

Over our years of knowing each other and learning together, we've expanded into becoming business partners. He's been a limited partner with me in two multi-family property acquisitions in Memphis, 2017 and one in Birmingham, 2018.

This book is an introduction into the world of multi-family property syndication. It's a topic that sounds more complicated than it is. With a little background knowledge and the right perspective, anyone can invest in multi-family properties, which are any residential properties that can house five or more families.

If you have extra money that you're looking to invest in alternative assets, this book is going to offer you an option for that. As Rey can attest, this is a passive investment that can be done at any time from any place. It's a critical path to consider if you're looking for options.

I could think of few people better qualified to write about passive multi-family investments than Rey. He's not someone trying to make money selling the secrets of success without first following them for himself. The reason Rey is able to write this book is that he's used the very same strategies he's talking about here to invest his own money profitably.

Rey was a military guy, often leaving for years on deployments around the world. By his own admission, this was an obstacle with his own investing for years. But, when he got into multi-family property investments, he managed to do that while he was abroad. He didn't even have to see or visit the first property he invested in to know it was a good deal. All you really need is the numbers, information about the team, the deal, and the right calculations to get an idea on the value of a property. It's hard to get much more hands-off than that. If he can do it, so can you!

This is a book geared towards busy professionals or anyone who has things going on and doesn't want to spend a lot of time on their investments. Whether you're enjoying your retirement too much or you just don't have the time to spare at all, the time commitment is not necessary with syndication deals.

You can do this as a professional or career investor as well, but it's not a requirement. Once you're invested in a deal, you can be hands-off and act as a purely passive investor, sitting back and reaping the benefits of money well placed.

This is an exciting book! Rey and I share a passion for teaching people about multi-family real estate investments. As an author myself, I'm happy to see him stepping into this as an avenue to reach more people and create a reference point for people looking for investment options.

The main reason this book is exciting to me is that Rey is one of my own success stories. Utilizing my program and what he learned from my real estate underwriting courses, he applied that knowledge and his own existing understanding to find, analyze, and close on a very successful multi-family property deal. Rey had many years of investing in single-family properties before he bought into his first multi-family deal. While he went into the red a few times with single-family investments, he's never once gone into the red with multi-family properties. This is a sign of smart investing on his part, especially putting in the work to check and analyze deals before he put his money into them.

Rey is a guy who puts his money where his mouth is. He only tells you what he's already learned and found useful in his own investments, while drawing from real-life experiences. Ismael told me once that he was profoundly affected by the book "Rich Dad, Poor Dad," which is a book that greatly changed my own attitude towards money as well. We both share a passion for developing streams of passive income and teaching others how to do the same. That's the kind of person I can get behind and support.

I hope you're able to read this book and realize that multi-family property investments are within your grasp. They're not just reserved for professional investors or real estate industry giants. Anyone can do it, so long as you're willing to put in a little work at the start. Once you're in, it's one of the easiest investments to maintain and grow, all while doing almost nothing!

If an investment like that is just waiting for you… Why not give it a chance?

Michael Blank

Full-time Entrepreneur, Investor, and Coach

www.themichaelblank.com

Introduction

There are so many investments you can get into. Rather than putting all your eggs in one basket, a wise investor diversifies their portfolio to include investments not dependent on all the same economic factors. A healthy mix of stocks, bonds, and alternative assets does wonders. Real estate investments fall into that last category of alternative assets.

In this book, you're going to learn more about my preferred type of real estate investment: the multi-family syndication. This is a reasonably stable investment that offers a solid return and allows you to be a passive participant, provided you put in the work upfront when looking for an investment team and a property deal.

My Experience & Education

Let me start by saying I am not an expert real estate mogul. I didn't grow up doing real estate, nor do I have extensive work experience in the industry, but I have always had a passion for real estate (Monopoly was my favorite game when I was growing up!). When I was a kid, I distinctly remember moving into a rehabbed home that my parents bought. They were just your average working-class people, but they worked hard to make sure we had a great place to live. Their work ethic and the way we celebrated that home inspired me to work as hard as I could to give my own children more.

Despite having an MBA, I never formally studied real estate; the MBA was directed more towards international business. My real estate investment education came primarily through reading on my own and partnering up with others that did have significant knowledge and experience. The most influential book I read was right after getting my Commission as a 2nd Lieutenant in the U.S. Army: "Rich Dad, Poor Dad" by Robert Kiyosaki. This book fundamentally changed the way I looked at money and investing. It opened a whole new world of finance for me.

Once I became more interested in real estate, I started reading real estate investment books from everyone I could find. I read voraciously to learn everything I could before jumping in for myself. Reading is still a significant part of my life today. I continue learning what I can to help me improve my own investments, manage my money better, and get more out of my finances.

The reason I wanted to write this book is to help you realize that you don't have to be someone special or a long-time industry veteran to get started in multi-family real estate investment. You can do it at any experience level or with any background if you take the time to learn how to do it right.

My Early Investing

As a family, we had bought and moved into our first home in 2004. Previous deployments, including a combat deployment to Afghanistan during OPERATION ENDURING FREEDOM, and a 10-month long temporary-duty assignment to Colombia, had made it seemingly impossible for years. Once I found my groove in my military career (and had a little extra money in my pocket), I started looking to invest in real estate. It took me until 2005 to get stable enough in my location where I could buy an investment property. I did what most of us think to do in the beginning: I mortgaged a single-family rental home and managed it myself. I bought two properties that year: 1) a fix & flip and 2) a property that I personally managed.

The income was okay (when the property was occupied), but vacancies were a big issue; and as soon as I wanted to start scaling, I realized it wasn't going to work out. *My biggest problem was the inability to get* *things done when I wasn't physically there.* The great recession scared me out of buying between 2008 and 2011, which is one of my biggest investment regrets to date, one I won't make in the current recession. A mix of market paralysis and overseas assignments over this time kept me from jumping in again.

In 2012, I bought another property while I was still overseas. This was truly a fantastic investment (and it still provides me money to this day!). However, there is a flaw in all of this single-family property investing: ***<u>You must buy often in order to make significant income, and buying right takes time.</u>***

The more single-family properties you own, the more likely you'll need to hire a property manager (unless you're trying to make the investment of properties your full-time job). As a Soldier who was regularly deployed all around the world, I couldn't spend a lot of time managing properties. Property managers don't come cheap, especially if you only have a few houses for them to manage. If your properties are in different locations, you may need multiple property managers. ***You must get a great property manager if you want single-family houses to be a successful investment because a bad manager can sink an investment quickly.***

It didn't take too long for me to decide I needed to switch my focus. My last single-family purchases were in 2013 when I bought another two properties. Later that year, I discovered that I did not have to buy a multifamily property by myself. It was the beginning of my multi-family journey, and I've never looked back. As you read on, you'll understand why!

Transitioning to Multi-family

I really started looking into multi-family investments in late 2014. I founded MI Real Estate, LLC that year when I decided I would make a future career out of real estate, rather than treating it as just a passive investment. At that point, in addition to investing in single-family properties, I was also lending money out of my Self-Directed IRA account and business to hard money lenders, which provide short term, higher-interest loans to those that can't get traditional financing or need the cash in a hurry for a short period of time. While profitable, the lack of tax benefits from lending money and the desire to get more hard assets drove me towards to multi-family. From 2015, I studied multi-family investing and learned as much as I could. In late 2016, I joined my first passive investment team.

This is a deal I managed to do during my last overseas tour in El Salvador. I was a completely passive investor, so I didn't need to be involved in day-to-day activities and just checked up on the numbers from time to time. This was critical because as the Army Attaché, there was absolutely no way I could be more involved. I was away for two years, and upon coming back in 2018, I quickly jumped into another deal as a passive investor. Today, I'm investing more often as an active investor, a general partner (GP), also known as a co-sponsor, rather than a limited partner (LP), or passive investor. I closed my first deal as a GP in July of 2019 and a second in January of 2020. In July 2020, my partners and I closed on another 90 units – the COVID19 crisis and recession have created short-term havoc, but also long-term, generational wealth building opportunities to those willing to stay focused.

CLOSED

Reflections

As I reflect on all of my real estate investments, I can say I’ve done best for myself through my multi-family investing. This is not to say that single-family investing was a total loss. In fact, I still have a couple of single-family properties in my portfolio that do very well. However, I've only had negative cash flow, albeit minimal losses, on single-family properties. Early last year, I sold a single-family property in San Antonio, TX, which had been vacant for over 5 months. The biggest problem with that property was that the property manager began to underperform, and I was in the middle of returning from overseas and could not dedicate any time to managing him. The tenant vacated in August 2018, and when it didn't rent for three months, I decided to sell it and reinvest the overall profit into multifamily.

While establishing my multi-family investing, I’d been juggling a few things at a time. I was overseas for a time and then worked in a hectic job at Unites States Southern Command in Doral, FL, until I retired in late 2019. Even though I had a busy full-time career, I was able to manage these investments passively and still see my money retain its value and grow.

I am truly passionate about helping others, especially servicemembers, and have the confidence and knowledge to help them make the leap of faith to investing in multi-family sooner, rather than later. One of my biggest regrets is “seeing the light” as late as I did. It is one of the principal reasons for my writing this book.

Again, multi-family doesn’t have to be your full-time job. You can do it even if you’ve got a lot of other responsibilities pulling at your time and attention. In addition, you don’t have to “graduate” from single-family investing to passively invest in multi-family. I cannot stress this enough.

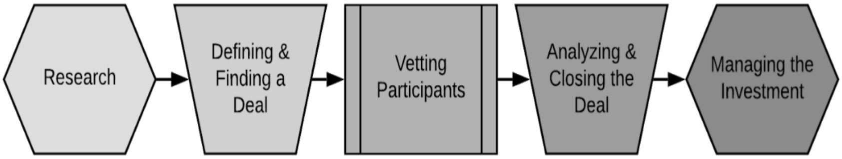
What to Expect

Investing in multi-family syndicates is more of a process than buying a single-family property. You’ll be working with multiple people, there are more moving parts to the deal, and the capital requirements can be intimidating for some. But you’re not bound by geographic restraints for your investment, and you can be a passive investor once you’ve settled into the deal. Thus, investing in multi-family syndications enables you to invest in real estate where and when it makes the most sense (#InvestWhereItMakesCents).

I’m going to take you through the multi-family investment process step by step. This book focuses mainly on syndication deals, but we’ll touch on some of the other ways you can invest as well.

The general steps of the process are researching and understanding the process, establishing your investment criteria to find a suitable deal, vetting the people involved in the investment team, analyzing and closing on a deal, and following up with passive management.

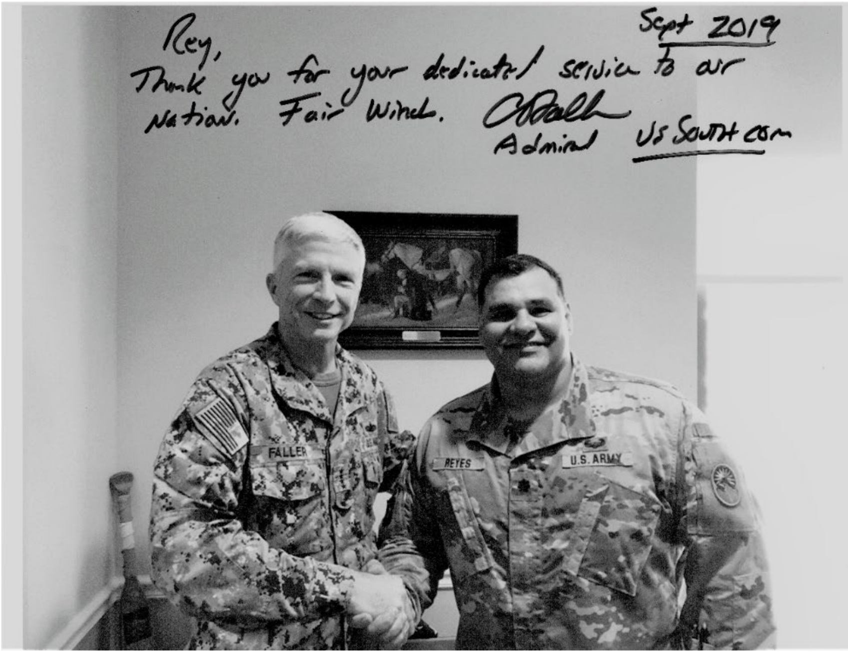
I'll be using this graphic to help you understand where a specific chapter fits into the whole investment process:



By the end of this book, you'll have a better understanding of what a real estate syndication deal involves and how to get started on your own deal. Although the process looks complex upfront, it's not as difficult as you might think. If you put in some legwork, you can get started with a syndication in no time.

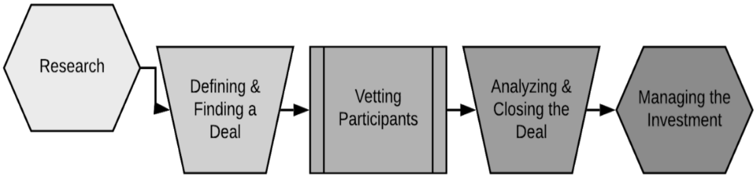
Final Note

As a 28+ year military retiree, old habits die hard. At the beginning of each chapter, you'll see a section labeled "**BLUF**." This is a term that anyone affiliated with the U.S. military will understand immediately: "Bottom Line Up Front." We use the **BLUF** to brief our superiors quickly because they're busy and have other important things to do – too much to do, not enough time. Within this book, the **BLUF** consists of bullets that highlight the most key takeaways within a certain chapter. I realize you're also a busy person with a lot of other things pulling on your attention. That's why I've included these little sections to give you a short overview and to help you understand what's in a chapter without having to read the whole thing first.


Sept 2019
Rey,
Thank you for your dedicated service to our
Nation. Fair Winds.
Admiral US SouthCom
FALLER
REYES
U.S. ARMY

Chapter 1

What Is Syndication?



BLUF

1. Real estate syndications involve the consolidation of capital
2. Syndications require a sponsor-team and multiple investors
3. Widespread internet access has made syndications easier

Expanding Your Portfolio

Real estate investment provides you with multiple options. If you're interested in something that won't necessarily take up too much time but can still give better returns than the average vacation home rental unit, syndication is worth a look.

To make a recession-proof portfolio, you want a few different types of alternative assets to counterbalance your stocks, bonds, and traditional assets. Real estate is a unique asset in that you get paid regularly from it, you get more equity with every debt payment you make, it can offer significant tax benefits, and it typically appreciates in value over time. As a tangible asset, real estate is fairly illiquid, meaning it shouldn't make up your entire portfolio, but it offers some security to you since it's more than just a piece of paper.

Real estate investment offers a few different alternative asset types, many of which can be acquired through syndications. Syndication specifically can be worth looking into because of the passive role available to real estate investors and the ability to access more purchase options. Real estate syndication gives you the benefits of a managed property investment without a hands-on commitment or blind acceptance.

As you go through this book, keep in mind that I'm not an attorney, accountant, tax professional, or otherwise. Make sure you're treating this as a learning resource and not as a source for legal advice. I have a lot of personal experience with multi-family real estate investments over the years, and I'm sharing what I know from my own experience.

Many real estate investments for multi-family units and commercial real estate are set up as syndication deals. With that in mind, here are the basics of real estate syndications.

Defining a Syndication

In official terms, a syndication is defined as:

"The pooling of the resources of a group of individual investors to acquire or develop an agreed-upon real asset."

This means is that syndications are groups of people working together on a real estate project. With very few exceptions, each syndication is formed around a specific real estate project that's already defined in the deal.

The project can be anything involving a real asset.

The most famous example of a syndication was from 1961. The Empire State Building was purchased as a syndication with more than 3,000 individual investors contributing. Harry Helmsley was the man in charge of the deal, and he rounded up all the investors along with his own financing in order to make the purchase happen.

Syndications allow you to make a larger investment than you would have been able to as an individual. If you want to undertake a money-making real estate project you can't afford, a syndication deal can help you make it happen.

Who's Involved in a Syndication?

At the very least, two people are involved in a syndication. Each deal has a sponsor and an investor. Most deals rely on multiple investors and a single sponsor. In the Empire State building example, Harry Helmsley was the sponsor, while the 3,000+ other individuals were investors.

Sponsors are the ones on the ground doing most of the work involved in making the investment a success. They often contribute some money to the syndication, but they'll invest more through sweat equity than monetary capital.

Investors contribute capital to a syndication. Their obligation is mostly finished after they've contributed, because they do little to no work on the project itself. In essence, investors play a passive role in the syndication, while sponsors are the active members.

This is only a brief mention of a topic that deserves its own space. There are often more parties involved in syndications. They don't all neatly fit into sponsor or investor categories, but they act in support roles to one of the two groups and provide vital services to the syndicate. You can learn more about all the members in a syndication and their roles, responsibilities, and benefits in chapter two.

Typical Legal Structure for Syndications

To protect everyone involved in the deal, syndications are not done unofficially. There should be a legal structure in place that illustrates the responsibilities, risks, and compensation for everyone involved. Most of the syndications are set up with one of these legal structures:

- Corporation
- Limited liability company (LLC)
- Full partnership
- Limited partnership

Each structure has its own benefits, challenges, and tax implications. This is something you should evaluate and understand before you get involved in or start a syndication. In chapter 3, we'll go over each option a little more thoroughly with a focus on the tax advantages and when they may or may not make sense, as well as the different types of real estate syndications.

A New Take on Syndications

Syndication deals have been taking place for more than a century in the US. They started to grow in popularity in the 1920s before dying off again during the Great Depression. However, in the early 1950s and throughout the 1960s, there was renewed interest in real estate syndication. The most significant difference between then and now is the demographics of the deals.

During the 1900s in general, investors and sponsors who formed a syndication agreement tended to be those in upper-middle-class or upper-class socioeconomic positions. You had to be able to invest a large sum of money or contribute valuable knowledge and experience. Most syndication deals came about from people who rubbed shoulders with the wealthier members of society.

If you didn't have access to the people with the money, and you didn't have the money for yourself, syndication wasn't an option. Thankfully, that's all been flipped on its head since the advent and mass popularization of the internet.

The Internet's Effect on Syndications

Never in the history of humankind have we been able to connect to so many people around the world so easily. This connectivity has changed the world and influenced every aspect of our lives, including how we do investments and make deals. The internet's influence has revolutionized investing overall, but revolutionary changes have taken place in real estate investment.

Syndication deals were somewhat common before the internet, but the growth in popularity of the internet brought people closer together and allowed people to connect with diverse groups easily. The internet has made it possible for more people to learn about and organize a syndicate.

Instead of waiting to bump into the right person, you can go and find them online. In addition, you can seek out a large number of people with a little bit of money, instead of going after a few people with a lot of money. It's taking the Empire State Building syndication model and spreading it around for even more people to access.

Today, you can get connected to existing syndication deals or form your own team much more easily. The internet facilitates every part of the deal, from start to finish. Arguably the largest way syndications have been affected by the internet is through the beginning of crowdfunded deals.

The Impact of Crowdfunding

The internet is an incredible tool to connect large groups of people. When you can't find a single investor or small group of investors to contribute to your investment plan, you can source the funding from a crowd of strangers instead.

Crowdfunding is taking small capital investments from a large group of people through an online platform. It's usually done at the start of a venture, but it's also occasionally done when a business needs capital to expand or do something new. The financing model has been used in nearly every industry, especially for new online startups, but it's found a place in real estate as well.

Real estate syndication deals can be crowdfunded to great success. No full-page newspaper ads necessary. You'll need a solid legal contract that puts dynamic and fair terms to the deal, but there's no reason a lot of different people shouldn't have access to small pieces of the pie. In most syndication deals, there's enough to go around.

Because of the availability of crowdfunding, you don't have to worry about funding projects a little larger than you would normally take on. This is how you can take on more lucrative multi-family property deals instead of focusing on the smaller single-family units.

Syndications vs. Real Estate Funds

If you're at all familiar with real estate funds, a lot of this sounds familiar right now. Funds and syndications are similar in their mechanics, but they differ in one key aspect:

While syndications raise capital for a specific, identified opportunity, real estate funds raise capital <u>before</u> identifying a specific opportunity. There is a type of syndication called a *blind pool syndication* that doesn't focus on a specific asset, but instead identifies the class of asset that will be sought out, but these are less common.

With a real estate fund, you don't know exactly what you're getting into until you've already contributed to the investment; many funds don't actually invest in real estate; they invest in Real Estate Investment Trusts (REITs), which are publicly traded companies that own, operate or finance income-producing real estate and are subject to similar market swings as stocks; or they invest in real estate operating companies. You're investing a lot into the track record, experience, and reputation of whoever is managing the fund.

Syndications don't rely so much on the manager's ability to find a good deal. Investors are presented with all the data upfront, affording them a degree of control over their investment. There's little room for surprise. Even if funding sources, investment terms, and other factors are the same, that one point of difference is huge.

Why Consider a Syndication?

By yourself, you have limited resources. When you work together with others, you can get involved in exponentially larger projects that end up being a lot more profitable. Smaller projects are fine if you are risk-averse or just prefer to work alone; however, higher risk leads to higher rewards.

There are two main reasons I think you should consider real estate syndication as an option:

1. *You don't have to be hands-on*

If you don't have the time or ability to manage the project yourself, you can participate in the deal as one of the investors instead of the sponsor. Additionally, if you have a trusted sponsor taking care of things on the ground, you won't have to think about it daily.

From my own experience, this has been a better way of doing it than focusing on multi-family units in your local area. You can find better deals if you expand your search nationwide. In late 2016, I had the opportunity to invest in a 100+ unit multi-family portfolio in Memphis, Tennessee. At the time, I was stationed in El Salvador for a two-year stint, so there was no way I could pop over and check out the project as it was going on.

The project sponsor was very trustworthy and experienced. He already had a great reputation, and he presented me with a full data packet giving me all the data I needed to vet the property myself. I ended up buying into the syndication, and it's worked out well for me.

2. You can do a lot more

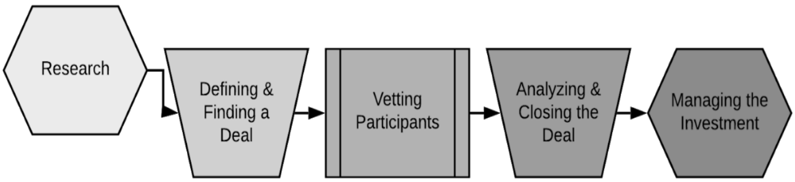
Realistically, you probably can't purchase and manage a multi-family property as a working professional. It's difficult for one person to get the capital alone. Even if you do, it's also challenging to keep the place running smoothly to ensure you get some return on your investment. In fact, some of the better investments include buying run-down assets from people who tried going at it alone and improving the property's profitability.

Syndications help you raise a lot more capital so that you can acquire a higher value asset. Multi-family real estate investments are much more realistic through syndication than through your own individual funding. Banks don't like to give multi-million-dollar loans to the average Joe or Jane with no experience for a real estate project, but with a syndicate to back you, you may not need a loan at all, or you can get by with a much smaller one.

Is a syndication right for you? Could it be a good addition to your portfolio? I hope this book will give you the information you need to answer those two questions. If you do end up with a few more specific questions that aren't addressed here, check out www.mirealestate.us for a bit more about syndications and multi-family investing. From the website, you can also find links to follow me on Facebook, Twitter, Instagram or YouTube.

Chapter 2

Key Team Members in a Syndication



BLUF

1. Sponsors manage the assets during the agreement
2. Investors are passive participants
3. Preferred returns to investors get priority in payouts
4. Syndication teams should include advisors

Two Main Parties in a Syndication

In chapter one's "Who's Involved in a Syndication?" section, I mentioned who the main participants are in a syndication deal: the sponsor and the investors. Because there's a lot you should know about both, I've dedicated this chapter to help explain the roles, responsibilities, risks, and expected benefits of each in more detail.

Sponsor

Sponsors in a syndication are also called **operators** or **principals**. They play a highly active role in a syndication deal. There is typically only one sponsor, whether it's an individual or an entity like a company. Individual sponsors are most common.

Responsibilities

Before the deal even begins, a sponsor's work starts. They are the ones who source the opportunity. In practice, this means finding a valid project and putting together a deal. Sponsors may work together with one or more of the people they intend to invest with, but they're mainly doing the scouting and setup work alone.

Sponsors often initiate the syndication deal to fund an otherwise unattainable opportunity. They need capital, so they work with a team of investors to fund whatever's needed for the project. While the sponsor is expected to put in some capital of their own, they may not have to put in as much as the investors. It's important for them to demonstrate they also have something to lose if it fails.

Where the sponsor lacks in capital investment, they make up by putting in their time, effort, and hours of work (sweat equity). Not only do they find and initiate the syndication, they're also in charge of managing the operation, usually called **asset management**. The sponsor is directly responsible for day-to-day management to make sure the project continues as planned and produces a profit for everyone involved.

Sponsors are trusted to do this because of their experience, skills, knowledge, and track record with similar projects. A trusted sponsor should have the right mix of experience and proven success to give the project a better chance of becoming profitable. Sponsors leverage their intangible assets to gain the capital needed for the project.

Risks

More is at stake for the sponsor than the investors. They deal with both financial risk and the risk of reputation loss.

Although sponsors don't normally contribute as much as investors, they still stand to lose that amount if things go sour. Whatever the sponsor invests, including in finding the opportunity in the first place, is at risk just like any other investor.

Reputation loss can be significant for sponsors. They're trusted to sponsor a deal because of their good track record. A big loss can ruin that reputation and get in the way of any future investments they want to do or financial moves they want to make. One bad deal might make them less investable for years, and it can be hard to build that good reputation back up.

The reason for the syndication's failure will play a part in this reputation loss. Bad choices and mistakes made by the sponsor while managing the asset will be particularly damaging. However, failure due to difficult outside circumstances, such as the real estate market crash in 2007, or the more recent COVID19-triggered recession, may not be as bad overall. Having said that, experienced and/or cautious sponsors and investors had been expecting a recession for quite a few years and should have underwritten their acquisitions accordingly - certainly, my partners and I did.

Expected Benefits & Compensation

There are three ways that sponsors can typically expect to make money through a syndication:

1. Management Fees

In exchange for their ongoing work managing the investment asset, the sponsor is paid a management fee. The fee should be set in the operating agreement (we'll discuss operating agreements in more detail in Chapter 11). Depending on what's agreed, the management fee may be paid before or after investors get their preferred returns (more on those later in this chapter).

2. Gains

After investors are paid, and the management fee is covered, any remaining profits are dispersed to investors and sponsors based on the terms outlined in the agreement. Usually, a more substantial chunk of the profits is given to the investors, such as 50 – 70%, while the smaller amount is paid to the sponsor. However, this is still the primary way that sponsors make money on a syndication deal, as their share in the profits is usually not split between as many people, if it's split at all.

In this way, sponsors are incentivized to do their best. In case there is no extra profit after preferred returns are paid out, sponsors will not receive money. The priority is placed first on investors receiving their preferred returns before any other payouts can occur.

3. Asset Sale

Once a syndication asset is sold, sponsors share in the profits of the sale. This is often based on their equity at the time of sale, but the specific terms should be laid out in the operating agreement.

Investors

Syndication deals are built around investors. These are the people or entities that bring the capital to the project. There can theoretically be any number of investors involved, with some limitations. For syndications, we must distinguish between accredited, non-accredited, and sophisticated investors. According to the Securities & Exchange Commission (SEC), Accredited Investors are:

1. Persons with an individual income greater than $200,000 in each of the two most recent years or joint income with spouse greater than $300,000 in each of those years, with a reasonable expectation of reaching the same income level in the current year; or

2. Persons whose individual net worth, or joint net worth with spouse, is greater than $1 million USD (excluding the value of primary residence).

Non-accredited Investors are persons that don't meet the SEC definition of an accredited investor.The SEC defines Sophisticated Investors are non-accredited investors that, “have enough knowledge and experience in business matters to evaluate the risks and merits of an investment.”

Because of SEC regulations, specifically “Regulation D,” syndication deals should not involve more than 35 sophisticated investors (Rule 506(b)). They can work with an unlimited number of accredited investors (Rule 506(b) and 506(c)).

While this is the federal standard, many state laws offer exemptions to this limitation. States with exemptions typically allow any number of non-accredited investors as long as the investment and the investors are located within the state.

Not all syndication projects need an enormous investor pool, but those that do need to be a little more selective about who they work with. Your legal advisor can help you sort this out to make sure nothing is happening that will cause any issues with the SEC.

Responsibilities

In most cases, the investors don’t have a lot of regular responsibilities to fulfill. Upfront, they’re responsible for investing a certain amount of money and for paying fees to the sponsor who found, organized, and closed the deal. Depending on how the deal is set up, initial fees may be covered by the upfront investment money.

The appeal of investing is often that you don’t have to actively manage the project. Once you’ve invested, the sponsor takes over and does all the legwork. Unless the contract states otherwise, you can continue working in your profession while your money goes to good use elsewhere.

You should always be following up and checking on progress, no matter how much you trust the sponsor. Just because you don't have a stated responsibility to manage the investment doesn't mean you should keep your distance. Make a point to track the financials and understand what's going on.

Save surprises for birthdays and leave them out of your investments. If you're surprised by the numbers or blind-sided by something that you should have noticed, you're not investing wisely. Even from a distance, you can be close to your project. Keep in touch with the sponsor and seek out information and updates on a regular basis.

Risks

Financially, investors tend to take on greater risks than sponsors. Because the investors put in a more substantial chunk of the capital, they stand to lose more in the deal.

Real estate is a notoriously tricky market, especially in the US. While profits are relatively stable most years, things can change rapidly. Multi-family units tend to reduce the risk of a total loss, but nothing is free of risk.

Investors risk losing the capital they invested. If the syndication deal is organized correctly, there should be no further risk for investors.

Expected Benefits & Compensation

Syndication deals are set up to clearly outline the compensation an investor can expect to receive. This shows up in three distinct areas:

1. Preferred Returns

Investors are provided returns on the project's profits. The exact percentage is laid out in the operating agreement but is usually around 7-12%. Preferred returns, often part of in real estate syndication deals, must be paid out to investors first before any other separation of the money.

How each syndication calculates and pays preferred returns is decided in the operating agreement as well. Some may pay annually, while others pay monthly. One deal may offer compounding, cumulative returns, while another may not.

Consult with your own legal advocates before you enter or create any syndication deals. This is one of the issues that should be fully settled before any investors are signed on.

2. Gains

Once preferred returns are paid, the sponsor and investors split any remaining profits on a pre-arranged basis. This can be anything from a 70/30 split to an even 50/50 and everything in between.

Again, make sure this is clearly established in writing.

3. Asset Sale

If the syndication asset is sold at any point, the investors are paid back based on their equity ownership. This is pre-arranged when investors buy into the syndicate. When the property value appreciates over time, investors can expect to make a profit on the sale.

Other Key Members in a Syndication

Many people are involved in the deal, even if they're not directly sponsoring it or investing. These are your support team members that make sure you stay on the right track and don't get stuck in something bad.

Legal Advisors

There are a few legal advisors you should consult about a syndication. The bulk of your legal advice should come from:

- Real Estate Attorneys
- SEC Attorneys

Any attorneys you work with should have a lot of experience with real estate syndication specifically. Don't seek out advice from attorneys that haven't directly dealt with these types of deals before.

Syndications are legally complex. There are several state and federal regulations governing how they work. You'll also need a completely bespoke operating agreement, which will be drafted by an experienced real estate attorney. Even if the sponsor consulted with an attorney to draft the agreement, you should always bring in your own trusted legal advocate to look over the terms of the deal.

SEC attorneys are essential because of the nature of SEC regulations regarding syndications. The SEC is a complex entity that should never be ignored when you're dealing with any kind of investment. Work with both a real estate attorney and an SEC attorney with experience in syndications.

Tax Advisors

Before you get involved with or initiate a syndication, and while that syndication is ongoing, you need a tax advisor on your side.

Accountants and other tax professionals can help you get a grasp on the tax implications of your syndicate structure and the obligations of all parties involved. Tax law in the US is hard to navigate unless you have training and experience in it, so don't get too confident about your own abilities here.

Work with a certified tax professional or an accountant with tax law experience. Seek out someone who has worked with real estate syndication specifically, so that everything goes smoothly, and nothing jumps out unexpectedly.

With the changing nature of tax law, you need to keep a tax professional on hand to handle finances every year. Tax law changes could directly impact the tax obligations of your syndicate, requiring your direct attention. Make sure a tax professional or accountant is working with on the deal annually.

Compliance Officers

It can be worthwhile to recruit an auditor and other compliance officers relevant to your project. Depending on where you are, regulations around multi-family units may differ. Rather than paying fines or facing expensive fixes unexpectedly, compliance officers help keep things in check.

Your involvement with compliance officers can be sporadic if it's consistent. A compliance officer can help with sponsor and investor vetting, project vetting, continued project standards, financial auditing, and overall transparency.

Sometimes a mentor or advisor, in my case, Michael Blank, can help fill this role.

Real Estate Broker

Where do people find multi-family properties for sale? Many times, especially with larger multi-family properties, real estate brokers supply them. In fact, the best multi-family property deals never go on the market. These are also called off-market properties. For syndications, you're likely to use a broker to simplify the process of finding off-market properties.

Some syndications are never advertised due to SEC regulations. Brokers can help passive investors connect with those sponsors.

The other thing brokers can do is connect sponsors to their deals and assist with negotiations and acquiring the property in question. Local brokers are familiar with the market and know the ropes in their area. If a sponsor wants to get the best deal, brokers are usually the ones who can make that happen. Brokers may also facilitate the sale of the property after its value has appreciated.

Property Manager

Sometimes the sponsor will be the property manager, but not usually. In case the sponsor isn't the property manager, an outside company will be hired to fill that role. This company will take care of the rental properties on the day-to-day handling of employment contracts, dealing with tenant management, maintaining the property, etc.

All these services are provided in exchange for a property management fee. This is a monthly rate paid to the company for taking care of the property for the investors and sponsors. Property managers are paid before any other payouts are made for debts, dividends, equity, or otherwise. Their fees are considered a business expense for the syndicate.

Investor Relations Manager

Although these two terms seem unrelated, they're virtually interchangeable in the context of a syndicate. Investor relations managers usually part of the sponsor team. They advocate for the investors and ensure investors are getting all the information they need in a timely manner.

Generally, they're also involved in raising capital from investors as well and managing the relationship between investors and sponsors over the entirety of the investment period. If there are a lot of investors, or if the sponsor has multiple projects going on, investor relations can make it a

lot easier to keep track of everything and meet deadlines.

Investors need information, and they need to be able to get updates and feedback upon request. Sponsors also need a reliable way of getting feedback from investors, sending out information periodically, and managing crises when they occur. It's an important role, though not always strictly necessary, for a syndication to be successful.

Guarantor

If the syndicate will be taking on debt to purchase the property, the lender may require the naming of loan guarantors – individuals who can be held liable in the case of loan default. Often, the guarantors are those within the sponsor group or individual investors with a substantial amount of equity in the acquisition (usually 20% or more).

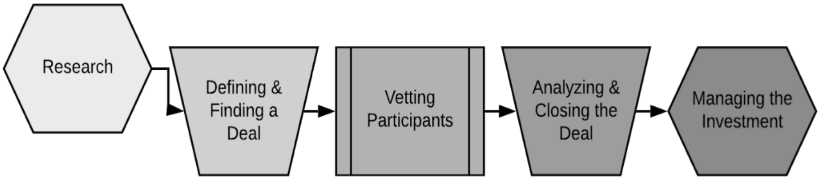
Lenders don't always require guarantors. If the loan amount is small enough or if there is a large enough down payment, they may be persuaded to forego individual guarantors.

Syndication teams are made up of a lot of different people and roles. Although the base team is just the sponsor plus the investors, the supporting roles play a huge part in ensuring the success of a syndicate venture.

20

Chapter 3

Tax Advantages of Multi-family



BLUF

1. Consult tax and legal experts before and during your investment
2. There are major tax advantages for multi-family properties
3. The legal structure shapes how investors are involved and legally protected

Taxes on Investments

Once you start investing in any way, filing your taxes becomes a whole lot more complicated. If your own personal finances are more complex, you can be certain that taxes involving real estate investment and syndications will be equally complex, if not more so.

Don't go into taxes or legal structuring alone. You'll be better off working with a professional who knows what they're doing and has direct experience with real estate syndication.

With that said, it's useful to know some of what you can expect from real estate investments. There are several tax benefits you can gain from multi-family properties, and you should at least be aware of them before you decide to move forward with investing.

Tax Advantages that Apply for Multi-family Properties

Most of the tax advantages you'll receive as an investor in a multi-family property come in the form of deductions and depreciation. Both categories of benefits reduce your tax burden, with the result being more money in your pocket that you can either re-invest (giving you yet another tax benefit in some cases) or use for another purpose.

Throughout the US, states and certain local areas have their own tax advantages or disadvantages. We won't get into all of that because it's beyond the scope of this book. If you want to know the specifics about what you can expect tax-wise from a particular investment property, you should consult an expert from that area to help you.

Always consult an expert for investment taxes. There could be benefits you didn't even know that a professional will be able to help you get and improve your bottom line. Often the expense of working with a professional will be more than covered by the savings you make on your taxes.

The information I'm providing here is not a full and extensive list of every tax advantage you have access to. It's a resource to show you some of the main tax advantages that apply everywhere in the US. Because I'm not an accountant (or tax professional of any kind), you shouldn't just take my word for it. It's always worth the cost to hire a tax professional or tax attorney when you're dealing with multi-family investments.

With that said, here's an overview of some of the tax advantages and benefits of multi-family syndication investments.

Insurance Deductions

Any insurance payments made to insure tenants, or the actual rental asset are usually deductible. Flood insurance, fire insurance, landlord liability insurance, employee health insurance, and other types of insurance are all generally deductible.

Interest Payment Deductions

A huge benefit for multi-family investors is the ability to write off interest payments related to the investment as deductions for tax purposes. This includes mortgage interest from acquiring the property, loans used to remodel or renovate, and even expense credit cards.

Consult with your advisory staff to get a better idea about what interest you can deduct and what your limitations might be. The Tax Cuts and Jobs Act of 2018 changed the limits for some investors, which is worth going over with your lawyer to understand if it may apply to you or not.

Expenses Deductions

Any expenses related to acquiring, owning, and managing your real estate investment asset are deductible. This includes everything from outreach efforts to gain new tenants, repairs and maintenance, services provided in the building, tenant retention efforts, and other activities. This can also include travel expenses incurred for the sake of running the business.

These deductions are exclusively for the business expenses of the property, not for your own personal expenses related to the investment. You and your lawyer or tax professional can investigate the Tangible Property Regulations released by the IRS to get a better idea about what you're allowed to deduct.

Note that completely new renovations and replacements aren't usually considered expenses. Instead, they fall under the next item on this list: depreciation.

Depreciation

For tax purposes, every fixed asset for your business has a depreciable lifespan. If you're not familiar with depreciation already, it's the steady loss in value of a fixed asset over a set number of years. It's a tax practice that reduces your tax burden on assets each year by only considering the depreciated value.

Most real estate investments are depreciable, apart from land, even though they usually go up in value! If you own the property or if you've entered a capital lease (not an operating lease), you can depreciate the fixed assets located on that land, such as buildings and landscaping fixtures.

The tax life of a multi-family asset is 27.5 years. To find the normal depreciable value of the asset over that time, you can divide its original value by 27.5. Depreciation reduces the taxable income from your asset, lowering your tax burden annually.

Cost Segregation Studies

You can't discuss depreciation without mentioning one of the best parts of multi-family: cost segregation studies. This is a practice that allows you to depreciate some parts of the property at different rates. It's not a trick, scheme, or loophole. All assets do not age in the same way. Assets with a shorter lifespan can be depreciated at a faster rate than the property itself, which can reduce your tax burden every year. Land is not depreciable.

As an example, new appliances installed in each unit will have a shorter depreciation time than the building in general, which is subject to a 27.5-year depreciation period. You could have those assets reclassified as 5, 7, or 15-year depreciable assets, which will increase your annual depreciation. Assets that depreciate faster will have their value spread out over that time period rather than the 27.5-year period, giving you considerably larger depreciable assets in the short term.

Why does this reclassification matter?

If you depreciate everything at the standard 27.5-year rate, you're missing out on the opportunity to put your money to better use today. Because the time value of money (TVM) means that money now is worth more than money later, you're potentially lowering your overall ROI. You could be re-investing from that extra cash flow now and growing it, whereas with normal depreciation, you would only have access to it in small amounts over 27.5 years. More importantly, most real estate syndications last 5-7 years, and refinancing a property resets the depreciation clock.

Working with an experienced tax segregation company can free up a lot more cash now that you can use immediately. Make sure the firm you recruit for the job has engineering, architecture, or construction experience, so they can accurately identify the function and lifespan of different parts of the building. A competent appraiser can get a more satisfactory result than an inexperienced team.

Cost segregation studies cost money. It's nothing to be afraid of if you're working with a high-cost multi-family property that you recently bought, renovated, or remodeled. The cost of the study is likely to be outweighed by the cost savings in tax in the year that it's done, but only if you're operating a large enough property, such as a multi-family.

Cost segregation studies seldom make sense for single-family properties. It's too expensive to justify in that case, since the cost may outweigh the actual tax savings in that year. If you have a single-family property, a low-value multi-family (under $500,000), or you plan to sell the asset within two years, a cost segregation study may not be viable.

Tax Implications from Syndication Structuring

Legally speaking, a syndication deal is not a true entity in and of itself. It requires some sort of structuring to make it a legal entity instead of just a group of people working towards a goal. It can take any form, but some are more common than others.

Limited Liability Company (LLC)

This is by far the most common form for a real estate syndicate. It limits the capital risk to investors, protects the members involved, and separates the members' personal finances from the investment itself. The real estate asset can be purchased and managed by the LLC. The sponsor(s) will be listed as managers, while investors are members.

Legally, it would be beneficial to set up a new LLC for every new real estate purchase. You don't want all your investments tied together, or they could all suffer from losses and legal troubles of one.

As far as taxes, having your personal finances separate from the syndicate's finances makes it a lot easier to manage each year. It won't be as complex, and the company may benefit from that.

With an LLC, you also have the option of listing different classes of members. You may want to give investors with more at stake a higher priority level than those who just paid in the minimum.

LLCs are taxed based on the adjusted gross income (AGI) of their owners, rather than being taxed as a separate entity. You will generally avoid double taxation issues, though that will be based on the exact legal structure of your syndicate.

Limited Partnership (LP)

Another common legal structure, syndicates are often formed as limited partnerships to take advantage of the liability limits for investors. One or more partners are designated as the active partners making the business decisions and movements (this is the sponsor), while the other partners are often passive investors who have minimal direct control over daily operations.

The benefit here is that investors have a liability limit that matches what they've invested. Under normal circumstances, investors won't be liable to cover any debts from the syndicate with their personal funds, though they can lose their entire investment that was given to the syndicate.

Corporation

It's not as common for syndications to be organized as regular corporations, but it does happen. The most significant benefit of a corporation is that it shields all investors involved from debts and other liabilities of the company. It's taxed as a separate entity, though, which can create instances of double taxation on personal income for investors.

Full Partnership

Where limited partnerships place legal limits on how much each person involved is liable, full partnerships do not. This is problematic for most investors, although the trade-off is that they'll have more direct control over the syndication.

No Legal Form

This is not recommended. While you can have a syndication agreement and operate the investment without any true legal form, it can lead to complications in the future. Not only will you have no real tax advantages in doing this, you also won't get the legal protections that a structure provides. It's always a bad idea to go into an investment deal without the terms, structure, liability, and roles of each person clearly identified on paper.

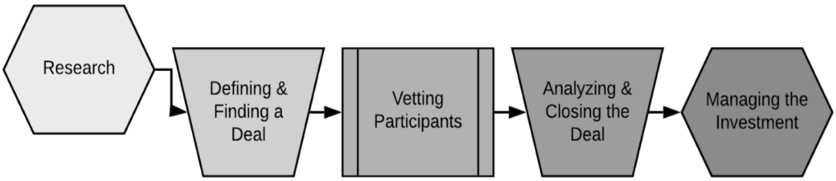
Taxes are complicated, and nothing in this chapter should be counted as legal advice, because I don't know your individual circumstances, and I'm not qualified to give that kind of advice. Consult with a tax lawyer, accountant, or other tax professional who can help you understand the best legal structure for your intended real estate syndication. There are a lot of nuances to this topic that can dramatically change your outcomes.

Having a general idea of your options is good, but you'll need legal advice and assistance before you make a real move. You'll also want continued tax help as you go on to make sure you're getting the full benefits that tax laws in the US give you. These are legal tools meant to help relieve some of your tax burdens, so you may as well use them whenever possible.

Whatever you do, don't join into any investment that doesn't have its terms on paper, and never sign a paper that you don't fully understand!

Chapter 4

Why Multi-family Over Single-family?



BLUF

1. Multi-family means 5+ units
2. You can scale quickly
3. Revenues for multi-family are less risky
4. Multi-family provides a more reliable cash flow

Choosing Residential

Residential real estate can be categorized into single-family or multi-family units. If you want to invest in residential properties, your next decision is which category to go for. Personally, I've done both, and I can safely say I prefer multi-family. I'll tell you why later in this chapter. But first, a bit more about each residential real estate types and what makes them so different.

Differentiating Multi-family and Single-Family Units

Single-family properties are individual properties that are built to house between 1 - 4 separate tenants or families. They can be anything from a traditional home to a condominium or townhouse. Even if the property or the house itself is very large, it can still be defined as single-family if it's only intended for 1-4 tenants.

Commercially, multi-family properties are defined as any properties that are built for 5+ tenants. Apartment complexes are the most well-known and often the largest examples of multi-family properties. As long as there are separate homes on the property and it's intended for five or more tenants simultaneously, it's a multi-family property.

In the case of a condominium or an owned apartment, a single-family property can be located inside a larger multi-family unit. Someone may own the building the condo is housed in while the condo is a single-family property owned separately.

Benefits Comparison

When compared to other real estate investments, both single-family and multi-family units share some benefits. There's always some demand for residential spaces, though the specific demand varies. Both also have a generally good long-term ROI, even when, or in many cases, because of the fact that you take out a mortgage to cover some or all the purchase costs.

Individually, each type of housing unit has its own benefits as well. Take a look at some of the major benefits for multi-family and single-family units:

Multi-family

- Revenue not dependent on one to four tenants
- Higher income from rentals
- Vacancies are not as devastating to income
- Greater control over unit value
- Lowering maintenance costs per unit
- Cheaper per unit to purchase
- Easier to manage than multiple single-family units
- Quicker to acquire multi-family units than multiple single-family units
- Lower property management cost per unit

Single-family

- Tenants often feel invested in the space (i.e., they stay longer in the space)
- Fewer maintenance problems
- Easier financing
- Steady value appreciation
- Easier to liquidate quickly

Challenges Comparison

Along with their benefits, they also share some specific challenges. The two notable shared challenges are higher mortgage rates and a dependency on residential tenants rather than corporate tenants. These challenges aren't as daunting as they appear and shouldn't be a deal-breaker for investing in multi-family or single-family real estate. Other sectors have their own difficulties, as we'll see in the next chapter.

The following are a few of the main challenges faced by each residential real estate type:

Multi-family

- Higher occupancy turnover
- Potential for tenant disputes
- More capital necessary for purchase
- Value appreciation based on property income and expenses

Single-family

- Vacancies mean no revenue at all
- Tenants may take more time to find
- Value determined by external circumstances

Why Choose Multi-family?

Everything has its own benefits and challenges. Those help you make the decision, but ultimately, you'll find your own reasons to invest or not. I think there are a few more compelling reasons to look at multi-family over single-family, outside of the aforementioned benefits.

1. NOI is consistent

Your net operating income (NOI) for a multi-family property is likely to be consistent, with the result being higher profits than you'd get from single-family properties. Not only are you getting rent from a lot of different tenants, but all their expenses will be spread out across the property.

Instead of thinking about multiple separate properties with their own problems, everything is in the same place with a lot of shared expenses. For example, you would only have one roof (or fewer roofs) to replace if a hurricane damaged your property, rather than having to replace multiple roofs on different houses. All your water, electric, sewage, etc. are connected to the same place, which simplifies everything. Most of all, you can manage all your units more easily because there's (less) travel involved.

NOI is going to increase when you reduce your operating expenses. If you were to compare operating expenses for multi-family versus single-family units with similar rent, multi-family is almost always cheaper to maintain.

2. Easier financing options

From the outside looking in, multi-family looks like it's harder to finance because it's more expensive. However, you have a lot more options for financing, and the overall cost per unit is lower. While you may not get a mortgage for the entire amount, you can bring investors into the mix with syndications.

Getting your funding from multiple sources spreads the risk around, so no one person is taking it on by themselves. In a syndication, the risk is shared by the sponsor and the investors with no single person set to lose more than they've invested. Single-family properties are not usually capable of benefitting more than one investor at a time, which significantly limits your options.

3. Potential tax benefits for contributing investors (including you!)

The structure of a multi-family property deal makes it possible to gain some tax benefits. This has already been covered in Chapter 3, so go check that out if you haven't already. Basically, the tax deductions and advantages you can get on a multi-family, especially if it's been financed, can dramatically improve your returns from the property.

4. Value is tied to NOI, giving you the reins

The NOI of a multi-family property is one of the leading factors in the value of that property. This means that you've got a lot of control over valuation. You can improve the building and services offered, which will lead to an increase in rent. As rent goes up, so does the value of your investment property. You can also reduce expenses through better management.

External factors do have some effect over valuation, but it's not as dramatic as it is with a single-family property. With single-family, the quality of the property and rent prices are equally balanced against the demand for homes in general and the demand for that home. You don't have nearly as much direct control over single-family property value. NOI is not a useful measure for single-family properties.

5. Get a lot more done, faster

It's easier to finance several rentals in a multi-family unit than to finance multiple single-family properties. For residential real estate, the more rentals you have, the better your cash flow is. Unless you buy a large portfolio of single-family properties at once in a commercial loan, you wouldn't be able to finance enough single-family properties simultaneously, because you'd need a separate mortgage for each one.

Multi-family properties include a lot of rentals under one financing option. Instead of looking at ten different single-family properties and applying for ten different mortgages, you can do it all at once with a 10-unit property. When you want to build your portfolio faster, multi-family is almost always the way to go.

What you invest in is your own personal choice. I've invested in both types, and multi-family has worked better for me. I don't plan on going back to single-family properties any time soon! There are real merits that make multi-family worth considering over single-family.

I started with single-family properties for a few years before transitioning to multi-family. Although some of my single-family properties worked out well for me, it became very difficult to scale up my investments because I had to either manage the properties myself or pay a high price for a good property manager. Vacancies in single-family units are devastating, so you must manage them well if you're going to turn a profit consistently.

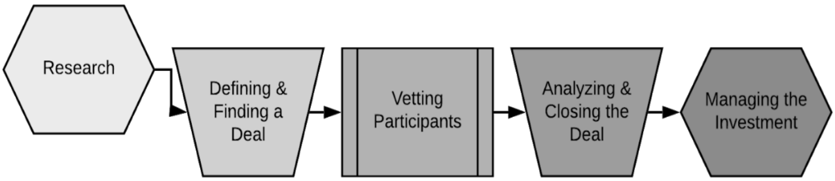
1st *single-family investment property – Bulverde, Texas*

From my perspective, multi-family is a better investment if you're looking to scale up at all. By the time you manage to get separate mortgages on each single-family property (if you manage), you could have easily purchased more units in a multi-family complex. Multi-family has better growth potential, which is one of the reasons I took a liking to it so quickly. I've personally decided to keep investing in multi-family rather than going back to get any other single-family properties.

36

Chapter 5

Why Multi-family Over CRE?



BLUF

1. There are major differences between multi-family and other CRE types
2. More control over property valuation with multi-family
3. Multi-family is not impacted by the same trends as CRE in general

Multi-family as a Part of CRE

- Commercial real estate (CRE) is a large sector that includes everything from tiny retail shops to shopping malls and office buildings. CRE is used for business purposes, making it explicitly non-residential. Within the broad label of CRE, there are four different subcategories: Office
- Industrial
- Retail
- Multi-family

Although multi-family is technically a type of CRE, it's worth evaluating how it compares to other types of CRE. It's somewhat of a hybrid category anyway, as the purpose of multi-family properties is to house residential tenants, whereas other CRE types work exclusively with non-residential clients.

There are some interesting comparisons to make between CRE and multi-family properties.

Benefits Comparison

CRE, including multi-family, generally has a greater income potential per property than single-family residential. There's a lot more research necessary to make sure you're getting the right property at the right time, but it's usually worth it in the end.

A lot of influential and wealthy investors have made a substantial chunk of their wealth from CRE, and there's a good reason for that. CRE can give you fantastic returns when compared to most other passive investments. Even if you invest in CRE with a syndication or other relatively passive role, you still stand to gain more than you would elsewhere, on average. Specifically, multi-family has its own benefits when compared to CRE in general:

Multi-family

- Recession-resilient with consistent demand
- Great cash flow
- Many individual tenants rather than one large tenant
- Minimal renovation needed between tenants to fit their needs

CRE

- More variety in market sectors allows you to diversify
- Increased barrier to entry means less investor competition
- Industrial real estate has lower overhead costs
- Longer lease periods with business tenants

Challenges Comparison

No investment comes without risks. There are a few challenges that both multi-family and CRE in general face, such as the capital requirements and greater regulation (although some sectors of CRE are way worse with regulation than multi-family). However, the challenges are unique to each specific type of CRE.

Multi-family

- Higher interest rates and down payments for purchase
- Increased potential for tenant disputes
- Property manager required, unless you have the experience and time
- One complication can devalue all your rentals at once

CRE

- Risk of long vacancies
- Retail sectors are experiencing trouble as online shopping increases
- High capital cost for investors
- Many sectors are heavily regulated; regulations differ between counties, states, etc.
- Less liquidity than residential properties
- Potential for unexpected tenant loss
- Renovations between tenants may be costly

Why Choose Multi-Family Properties?

If you asked me which I prefer, my answer would almost always be multi-family. CRE has its place in a diversified portfolio, but I wouldn’t put everything into it, especially if you’re inexperienced with real estate investing. For the passive investor, multi-family is less of a headache overall.

There are a few specific reasons that I’d say multi-family is the way to go.

1. People need a place to live before they need a space for their business

When times get bad, people still need a place to live. Even if businesses shut their doors and companies have layoffs, people have to live somewhere. It's not that you won't feel the effects of a recession or a bad local economy, but you're likely to be better insulated against it than a CRE investor.

The problem with CRE is that your clients are businesses, not people. The people who own those businesses and are employed around the area all need somewhere to call home before they need a place to do their business. Businesses may downsize or shut the doors before the people involved are truly unable to pay their home rent.

Economies go up and down, but housing is always a necessity. It's one of the necessities of all people, which makes it relatively safer than CRE. You can still run into problems finding tenants and paying the bills, but you'll probably be better off than if you owned other CRE properties.

2. Your income is less connected to a specific industry

One of the biggest downfalls of CRE is that it's strongly tied to specific economic factors. This varies by the type of CRE you invest in, but every type is bound to something.

For example, retail real estate is threatened by online shopping, while industrial real estate relies on specific companies keeping their production in-country rather than outsourcing. Office spaces are a little safer, but they still count on enough major businesses being in the area that need office space. If the company relocates, you may have trouble finding a new client to replace them if the climate isn't right.

CRE with service-based tenants, such as medical real estate, is arguably the safest type to invest in, as service companies can't be directly replaced online. Medical services are always in demand. However, medical real estate is heavily regulated and difficult to navigate, especially if you're not familiar enough with real estate investment. There are also fewer of these stable, high credit clients available to anchor your larger CRE buildings.

3. Cash flow comes from a lot of individual tenants, lowering your risk
Multi-family is the one segment of CRE that doesn't require large tenants connected to specific industries or economic factors. There's always some level of risk, especially if the local economy where the building is located is stagnating. However, the fact that you have many tenants who work across different industries decreases your risk and helps your cash flow, even if some portions of the economy face issues.

With multi-family, you cast a wider net for income. You can set up your rental rates so that your mortgage and expenses are covered even if your building isn't fully leased. The risk of a 100% vacancy is minimal, so your risk is lower overall. With CRE, you're too dependent on large clients for your income. It's riskier, because your cash flow will plummet if they vacate the property.

Large, anchor clients aren't always easy to replace. When you do have to get a new tenant, you may need to make tenant improvements as part of a leasing agreement. Individual residential clients don't have a lot of specific preferences that vary significantly from one another. Not everyone will like your place, but enough of them will that your potential tenant pool will be significant in most areas of the US. CRE tenants have more specific needs, unless you invest in co-working spaces, which are far riskier than multi-family.

4. Direct control over property valuation
As mentioned in the last chapter, multi-family property value is tied directly to the NOI. This means you'll have a lot of control over your

equity. By reducing your expenses or increasing your revenue, you can increase the value of your property without having to do any renovations or other physical improvements. This is fundamentally different to both single-family residential property and many other CRE properties.

When you're managing a multi-family property, you have some control over both income and expenses, and therefore the NOI. You can renegotiate utilities, install energy-efficient appliances and lights, switch service providers, or do any number of other things to reduce costs. You can also adjust the income you get from tenants to keep up with market rates.

If you find the right opportunity, you can significantly grow your equity without touching your mortgage, just by improving your NOI. This is the part of multi-family that's most appealing to bigger investors. More equity means you can get more capital for your next project and higher returns on investment.

5. Tech presents more opportunities than threats for multi-family

While tech brings a lot of impressive innovations to the market, it also cuts into CRE. Online shopping, automation, and non-traditional working arrangements all threaten different CRE types except for multi-family. Working from home, part-time or full-time, is becoming more common in order to reduce the costs of operating office buildings or large commercial spaces. None of these or other major tech innovations are set to make multi-family obsolete. It all comes down to my first reason: people will still need a place to live.

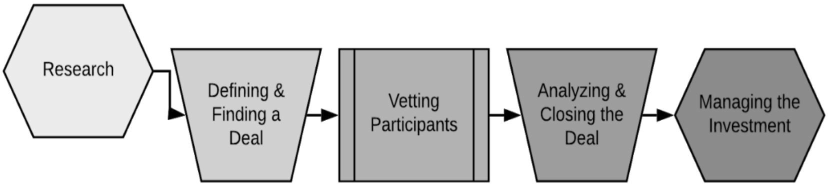
There are no tech trends currently that are set to disrupt multi-family. How people find places to live, how they negotiate the rent, and where they live may change, but no tech can directly replace housing in the same way it replaces jobs or businesses.

These are the main reasons why I think multi-family is the better part of CRE. A lot of investors do find success in CRE, but they generally diversify into a lot of different industries and business sectors to reduce risk. If you're just starting out in real estate investing, you probably don't have the capital to realistically do that. One multi-family asset in the right location generally has lower risk when compared to one CRE property. Therefore, investing in one might be the right choice for you.

If you want a little more insight as to why multi-family is my preferred type of CRE property, contact me at **info@mirealestate.us**, and we can talk about it a bit more.

Chapter 6

Key Terminology



BLUF

1. Multi-family uses specific ratios and metrics for evaluation
2. Know the terms before you analyze a deal
3. There are three general investment strategies: core, value-add, and opportunistic

Know Your Investment Terminology

Every area of investing has its own jargon that's used by people in the industry. From the outside looking in, these terms can sound a bit like nonsense, and they won't make anything clearer. If you don't already know some regularly used multi-family investment terminology, now's the time to get familiar with the basics.

Some of these terms have already popped up in this book. In case you didn't understand them fully, or you would like to see a simpler explanation, I've included them here again as a go-to reference.

Key Real Estate Investments Terms

Net Operating Income (NOI)

The net operating income is a number that tells you how much cash flow is left after you subtract the operating expenses from the operating income of a property. You'll see this number mentioned frequently in connection to the valuation of a multi-family property. The formula to find the NOI is:

Operating Income – Operating Expenses = NOI

To find the NOI, you need to know your gross operating income (GOI) and operating expenses.

Gross Operating Income (GOI)

To find the GOI for a property, you'll follow this formula:

Gross potential income – Vacancy and credit loss = GOI

The gross potential income refers to the total number of units on a property multiplied by the rent of each unit. This number is the total amount of rent that could be collected if all units are occupied and all rent is collected.

Vacancy and credit loss refer to any income that's lost because of vacancies, failure to pay rent, loss-to-lease (renting properties at lower than market rent), or giving rental concessions, i.e. move-in specials. It's difficult to get this information unless you own a building or have access to all the owner's financials.

GOI is the most significant part of **operating income**. The true operating income also includes income from other sources on the properties, such as vending machines, laundry facilities, extra services offered, parking fees, etc.

Operating Expenses

All expenses incurred by managing the building are included in operating expenses. Consider expenses like management fees, employee payroll, utilities, taxes, and other recurring costs. Don't include one-time costs or mortgage payments in this category.

Debt Service Coverage Ratio (DSCR)

This ratio is used by financial institutions and lenders to determine the viability of a certain loan on an investment property. It's found by dividing the NOI by annual loan payments. The formula looks like this:

Net operating income / Annual loan payments = DSCR

Most lenders prefer a DSCR of 1.25 or above. If this standard isn't met, you might not be able to receive a loan from all lenders, and the loan may have a higher mortgage rate.

Loan to Value Ratio (LTV)

A loan to value ratio helps lenders determine how much money to loan out for a specific investment property. The formula is:

Proposed loan amount / Property value = LTV

Many lenders also have LTV requirements. 75% LTV is generally the maximum a lender is willing to loan, as anything greater than that is a larger risk. The higher the LTV, the higher risk a loan is.

Capitalization Rate (Cap Rate)

The capitalization rate of an investment property refers to the interest rate return provided by the property. Simply stated, it shows what percentage an investor can expect to receive back from a property annually based on the original capital invested. The formula is:

Net operating income / Purchase price = Cap Rate

Cash on Cash (CoC)

The Cash on Cash ratio for a property is the ratio of pre-tax cash flow that an investor will likely receive for the funds they invest. The formula is:

Annual net cash flow / Invested funds = CoC

Average Annual Rate of Return (AAR)

This percentage shows the average return received on the initial cash

invested, considering changes in the property value, NOI, and mortgage paydown over a set period of years. The formula is:

[(NOI + property appreciation + principal pay down) / (# of years)] / initial cash investment = AAR

Internal Rate of Return (IRR)

The internal rate of return calculates the rate of return over the period a certain amount of capital is invested. It is similar to AAR in functionality, but unlike AAR, it works even if a property is refinanced or if an investor invests different amounts over time in the same investment.

While you can do IRR calculations manually, the formula is highly complex and cumbersome. Many simple tools exist to do these calculations automatically, to save you time and get the right answers. My favorite application for these types of calculations is Microsoft Excel.

Multi-family Real Estate Terms

Multi-family Property

A multi-family property is any property with separate residential spaces for five or more tenants. Though 2, 3, and 4-unit properties technically allow multiple families to live there, they’re not classified for lending purposes as multi-family properties.

Building Classifications

Every multi-family property is classified based on its value. The four general classifications are:

Class A

- Usually built within the last ten years or are substantially renovated.
- Charges premium rental prices.
- Attractive landscapes, rental offices, clubhouses, and other amenities.
- Highest quality construction, materials, workmanship, and maintenance.Offers high-end interior and exterior amenities.

Class B

- Built within the last 10-20 years.
- Charges lower rent range than Class A.
- Good quality construction with a low amount of maintenance issues.
- Amenities are more dated, and there are fewer offerings than with the higher-end properties.

Class C

- Built within the last 20-30 years.
- Charges lower rent range than Class B.
- Aging with more maintenance issues.
- Amenities are outdated, with fewer offerings than Class B.

Class D

- Built over 30 years ago, in poor condition, and in less-than-favorable locations.
- Charges lower rent range than Class C.
- Remaining systems and amenities (if any) have a short life.

Units

The term "unit" is used to refer to each separate housing area in a multi-family residential complex. A property with 100 units has rooms for 100 different tenants.

Core Investments

This refers to properties that are stable and income-earning without much room for growth or expansion. They have stabilized occupancy and are very low-risk properties that don't need any work to start generating cash flow. This is about as close as you can get to a passive earning investment property, but the returns are likely to be low as you won't be able to do much to add to the value. Normally, core properties are leveraged with 40% debt or less.

Another subsection of core property investment is the core plus property. The condition of the building and property is the same, but there is usually some opportunity for value growth through simple management or tenant changes. This could be reducing expenses, making light improvements, or even improving the quality of tenants. For core plus, investors expect to leverage 40 - 60% of the cost.

Value-Add Investments

As the name implies, value-add properties have good potential for cash flow once some value has been added to them. These can range from medium to high risk, depending on how much work is needed to generate significant cash flows. Investors often leverage 60 - 75% of the costs of acquiring and improving a value-add property.

Opportunistic Investments

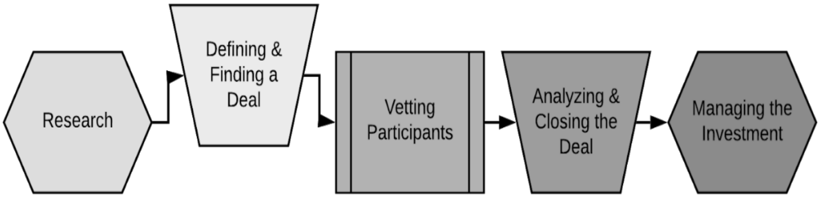
Considered the highest risk multi-family investments, opportunistic purchases often have little to no returns early on and are unlikely to produce cash flow initially. These properties might include ground-up developments, acquisitions of empty or unfinished buildings, and similar projects. 70% or more may be leveraged, depending on what the lenders are willing to provide.

There are a lot of terms to understand for multi-family real estate investments. If you’re not at least familiar with them, you might have more trouble evaluating a deal and making an informed decision.

Knowing is half the battle because it allows you to pick and choose properties based on metrics that actually matter.

Chapter 7

Determining Investment Criteria



BLUF

1. Multi-family is classified based on desirability and quality
2. Property location matters as much as building quality
3. Look at the current and projected numbers whenever possible
4. Base your investment criteria on what you want out of the project

Narrowing Down Your Search

There are a lot of multi-family units for sale in the US alone. How do you choose one that's going to suit you well? The start of the process is to decide on criteria you'll look at when you're choosing a property. Having some basis on which you judge every property helps you compare a few different options and make a better choice. Good deals are hard to find, but you're giving yourself the best chance if you lay out some pre-conditions before starting your search.

I'm going to talk about some of the main characteristics used to differentiate between multi-family units and how those can play into your investment criteria.

Multi-family Investment Classes

As briefly mentioned in the last chapter, Multi-family units are divided into different classes. These classes help you understand the characteristics of properties more quickly and differentiate between them.

The price of a property, its overall value and the rent you can charge for each unit will all be tied to its classification. Classifications are mostly just a rating system for investors, not a legal classification or definition. However, they do make it easier for you to narrow down your property search.

Class A

A Class A property is the highest quality of property available in the area. In its own market, it’s built to the highest quality standards with the highest quality of building materials. The buildings themselves should be relatively new, being built within the last 10-15 years. These are luxurious or semi-luxurious apartments with excellent amenities.

You’ll only see Class A buildings located in desirable areas. They likely have high-income tenants and very low vacancy rates. Class A will be some of the highest value rental properties in the local market. They will usually be managed professionally. Class A is considered one of the lowest risks, but it is more sensitive to recessions and economic downturns.

Class B

Just like Class A, Class B properties are on the higher side of the rental market. They’re not as high quality and luxurious as Class A, but they’re still above average for market rates and quality. These properties can be a little older than Class A, usually around 20 years old at maximum. They’re well-maintained buildings with attractive features and some amenities. With a little value-added work, investors can sometimes turn a Class B into a Class A or improve its value significantly.

Tenants in Class B are likely to have a stable, average to above-average income. Vacancy rates vary greatly based on the location, though many Class B properties are still desirable. They go for market-rate or slightly above market-rate in their area. Depending on the area and property, they may be professionally managed, or they may not be.

Class C

Usually, between 20 – 30 years old, Class C is on the lower end of the market. These properties are not high quality and will often need renovations and work to bring them up to a higher standard. The location of a Class C property is likely to be less desirable. Many Class C properties will have basic or limited amenities.

Tenants in Class C will have average to below-average incomes, and vacancy rates vary significantly. In some markets, Class C might have a lower vacancy rate because it's priced at or below market rates. However, you may have to do a lot of work to improve the value of a Class C and build equity from the investment.

Class D

Many investors aren't as interested in Class D properties, but they are still an option. These buildings can be 30+ years old and not well maintained. The quality of materials and construction may not be good. While they may or may not have structural problems, they will look their age and won't be situated in a desirable area. You're not likely to have amenities offered in a Class D property.

Tenant turnover in Class D is higher than in other classes, on average, but occupancy will be high on average as well. Rental rates in Class D are likely to be below market, while tenants have lower incomes. Parts of the building, such as appliances and previous improvements, may have a short life remaining, and there could be significant deferred maintenance.

Which Properties Classes Are a Good Investment?

Between the four different classifications, your risk tolerance, available capital, and location preferences will make the choice easier. While Class A units seem to be the most appealing right out of the gate, they tend to cost much more than other unit classes and may not be in as high of demand in all areas.

Many investors consider Class B properties to be a good compromise between risk and reward. They have the potential for added value to grow the investment. While Class A is almost guaranteed to minimize maintenance expenses, Class B has room to grow equity value through property/unit improvements while also supplying steady cash flow to investors and sponsors.

Class C isn't luxurious and doesn't have the highest rent prices, but it's more affordable and tends to have high occupancy rates. There is a lot of room for value add in a Class C as well, but it's a debate on whether the value addition will make a big enough difference for equity and NOI. The same can be said with Class D, although these might be riskier because of quality issues.

It's good to understand the property classes and decide for yourself what you might be interested in. There's no right answer here, so long as you pay attention to the unit in the context of the other points we're discussing below.

Neighborhood & Surroundings

Where the building is located and what's around it should be a big part of your investment decision. You can decide what kind of neighborhood and surroundings you're interested in investing in.

School Systems

If you're targeting families to rent your units, they're going to care about the school zoning. A bad school zone could deter people from renting, even if the units themselves are nice. Good school zones won't necessarily draw people in, but they won't actively deter them.

Questions to ask:

- What schools are the units zoned for?
- Are there multiple schools to choose from, or is there only one?
- How well are the schools in that zone rated?

Public Accessibility

In most areas, accessibility is a big issue. You won't be able to maintain high occupancy without good accessibility. Even upscale apartments where most tenants will be driving still benefit from being easily accessible.

Questions to ask:

- Is there public transit access nearby?
- How walkable is the area?
- Is it bike-friendly?
- How accessible is the property from the road?
- Where is the building in relation to a highway or main road?

Businesses & Workplaces

Apartments located too far away from areas of employment may be less appealing to prospective clients, although increased working from home due to the COVID19 health crisis may be mitigating this long-term trend. Generally speaking, commuting time can factor heavily into where someone chooses to live. You can't predict where all your prospective clients are going to be working, but if the building is located somewhat centrally to workplaces and businesses, it should be okay.

Questions to ask:

- How many industries and jobs are located around the area?
- Are there professional workplaces nearby?
- Is it easy to access areas of employment from the property?
- Do the workplaces nearby make sense with the rent requirements of the property?

General Neighborhood Conditions

Often, buildings will match their surroundings, whether that's a good thing or not. But even if the building is the shining star of an area, you may not want it if the area around is not good enough. It's a safer bet to invest in an apartment that's located in a good neighborhood that's well maintained. This is more likely to keep property value higher and make the units more desirable.

Questions to ask:

- Are streetlights working?
- How do other buildings and homes in the area look?
- Are the streets and sidewalks well maintained?
- Does the area look generally well cared for or rundown?

Shopping & Amenities

Residential areas should ideally be located close to shopping centers, even if only basic shopping is available. While many tenants are willing to go further for shopping, they do less frequently, such as going to a mall further away, they may not be as inclined to travel longer distances for necessities. You want a building that's as close as possible to basic necessities.

Beyond shopping, the building is likely to be more appealing if it's also located near outside amenities and attractions. Gyms, social clubs, religious facilities, and other public places are a welcome addition around the area.

Questions to ask:

- Are there grocery stores and shops for necessities nearby?
- Are there other shopping venues nearby?
- If the building doesn't offer a gym, where is the nearest gym?
- Does the area have public parks?

Examining the Macro Environment

Neighborhood knowledge is useful, but the direct local area isn't the only environmental factor to consider. You need to pay attention to some of the greater macro trends in the area to help you make a better decision. If you're not familiar enough with an area, you may consider partnering with someone local to the area to benefit from their insider knowledge.

These are the main factors I would recommend looking at.

Population Growth

How well is the city, town, or county itself doing in terms of population growth? If an area is not experiencing any population growth, growth is slow, or there's net population loss, that's not a good sign for the prospects of your multi-family housing property. Yes, you could still make money and keep a well-leased property, but it may prove to be more difficult than you want.

The exception to this would be an area that people desire to move to that does not have the right housing infrastructure to support the growth. However, this would largely be signified by steady growth in the area. If you catch the growth trend in the early years, it may look like slow or no growth. For a lower risk property, it's safer to pick a location that's experiencing steady population growth.

Low Unemployment

I've already mentioned employment in terms of a property's proximity to workplaces, but it's also worthwhile to make sure the property is in an area that has sufficiently low unemployment. If the area has high unemployment, it may be difficult to find tenants who can afford to live at the market rate and who will be able to consistently fulfill the terms of their lease.

High unemployment is not a good sign for the local area economy. When unemployment is on the rise, it may be a sign that market rents are going to go down as people lose their source of income. Stay away from areas with rising unemployment, unless the numbers are overall very low, and the rise is insignificant. Low unemployment leads to better future tenant prospects.

Gross Domestic Product (GDP) Growth

This usually goes hand in hand with employment trends, but focusing on markets with leading GDP growth is worth highlighting as well. As the saying goes: a rising tide lifts all boats. Put another way, a good property in a location with a stagnant economy requires operational excellence to provide investors a good return on investment; an average operator and property in a booming economy can perform just as well, if not better.

Technology Hubome of the best markets have a thriving technology hub. This is important because technology hubs are more likely to attract a younger and more affluent demographic that doesn't necessarily need a single-family house and would rather live near thriving city-centers.

Pro-Business Climate

Ideally, you want to invest in a pro-business state. This can look different, depending on the state you choose to settle in. In general, a pro-business state favorable for multi-family investments will have landlord-friendly policies, such as favorable tax structures and no rent control.

Real Estate Lifecycle

Do your best to understand where your local or target real estate market is in the real estate lifecycle before you invest – real estate markets don't always run parallel to an economic cycle! The lifecycle goes like this:

<u>Phase 1: Recovery</u>
After a recessionary real estate cycle ends, the economy starts to pick up again, including the real estate market. Real estate regularly goes through this lifecycle as the market changes over time. In the first phase, the market is just starting to recover and get on track towards growth again.

<u>Phase 2: Expansion</u>
Fears of the recessionary cycle are now firmly behind investors as the economy and the demand for real estate is growing steadily. It's a rush to get in ahead of the others and meet the growing demand for properties. At this point, there is generally a growing demand that is not supplied by existing properties, leading to growth in the market rents as well.

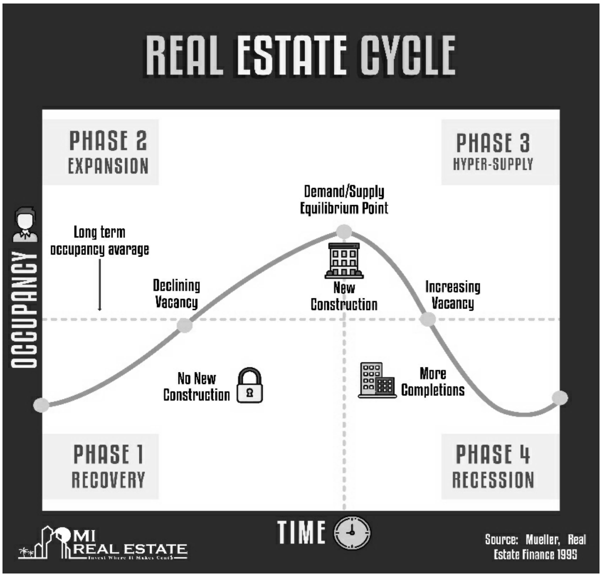
<u>Phase 3: Hyper Supply</u>
When expansion gets out of control, and outpaces actual growth, the result is hyper supply. At this point, enough developers and investors have come in that there are more properties being developed than there is a need for, resulting in empty properties and a growing real estate

bubble in the area. Demand may be steadily going up, but hyper supply means that supply is going up at a much faster rate than demand, with no likelihood of demand catching up.

Phase 4: Recession

As a result of hyper supply leaving too many properties for the available tenants, there is a recession in the real estate sector. This recession isn't always widespread in the general economy, but it means there is a retraction in the growth of the real estate sector in a local area. The hyper supply and ultra-growth period are over, with growth and supply going down sharply to be more in line with actual demand. You can enter the market during any of these periods and make a profit, but your strategy will need to vary depending on the exact time of entry. It's safest to enter during a time of recovery or expansion, but entering during hyper supply or recession could be riskier for you. Especially during hyper supply periods, you may pay an inflated price for a property that will have difficulty finding tenants and may end up losing value shortly after acquisition.

Here is a handy way to visualize the Real Estate Cycle and its potential investment impact.



Property Quality

Since you're looking at investing in the property, you should pay attention to every part of the property when making your assessment.

Parking

Every multi-family building should have some sort of parking arrangements or dedicated facilities. A minimum of 1 parking space per unit is good, but more is better to accommodate multi-car families and their guests.

Building Condition

A thorough inspection should be done to accurately determine the property's condition. If it needs a significant amount of work, ensure it's factored in during acquisition – some of the best deals are found in properties with significant deficiencies that can be purchased at a discount. If it's structurally sound, most cosmetic issues can be solved easily. While fresh paint and attractive design are nice, it's easier to change many cosmetic features over time, usually done during unit turnover, without having to make a considerable investment upfront. This would be a best-case scenario for a light value-add property.

Amenities

Many Class A and B apartments offer amenities. Some Class C properties offer limited amenities. Class D properties rarely offer amenities. Greater amenities can drive the rent price up but will also cost more in maintenance. If amenities are offered, the facilities should be checked to see what kind of condition they're in and how well they're holding up since installation. See how the amenities offered compare to those offered in similar buildings around the area.

Financials

The meat of your investment is the financial viability of the project. These are things you should look closely at when you're searching for a multi-family property. Decide what parameters you're comfortable with and use that as a set criterion for any investments you work with.

Occupancy Rate

How much of the building is full at any given time? Low occupancy rates indicate a riskier investment, while higher occupancy rates mean you're more likely to get your projected income every month. You can sometimes improve occupancy rates on buildings as you invest in them, but not always. Occupancy equals cash flow, so be careful with this one.

In many areas of the US today, 90% occupancy and above is normal. If occupancy rates are lower than 85% on average, the building is a higher risk. In fact, some of the lowest interest rate loans available to investors require at least 90% occupancy. While current occupancy may be high, it's important to understand historical trends. For example, if the property's rents are below market, raising rents may reduce occupancy.

Growth Potential

You'll get tax benefits from depreciating assets every year. But, if you sell the property for a profit, you could be taxed extra for depreciation recapture on your capital gains. For this reason and others, you have to make sure the building has enough potential for value growth that you can make up the difference you'll lose when you sell it. Class A may not be suitable for a short-term hold because of the lower potential for value growth.

Capitalization Rate

How long will it take you to earn back what you've invested? This is your capitalization rate. It's usually measured as a percentage based on how much of your original investment you'll regain annually. Of note, regardless of Cap Rate, if you can improve a property's NOI, you can increase its value. In fact, the lower the Cap Rate, the higher the property's new value, keeping the NOI the same.

Expenses

If you're able to access records of the expenses for a property ahead of time, this is a great resource. Expense reports will help you get a better grasp of the financials involved in a building and will give you a solid glance into any potential for growth. Lowering expenses can increase your NOI and the building's overall value, so seeing what the actual and projected expenses are is essential.

Rent vs. Market Rate

How does the current rental price per unit compare to the average market rate in the area? From this, you'll get a better idea about any potential wiggle room you have with prices. If the rate is higher than the market and the occupancy rate is good, it's a sign that the units or location are desirable.

Deciding Your Criteria

Based on the characteristics of multi-family investments, you can determine the criteria for investments you are personally comfortable with. Pay attention to a few key things:

Risk Tolerance

Your personal risk tolerance is the largest criterion for any investment. Decide how much risk you're willing to take in a multi-family property based on what you're trying to accomplish with the investment. If it's a close to retirement property, for example, you'll probably want a lower risk than if it's an earlier investment for wealth gain and balancing your portfolio.

Building Specifications

Decide what kind of multi-family property you're interested in. Do you want to invest in a stable Class B in a good neighborhood or a lower profit Class A with a bigger price tag? What are your upper and lower limits for units in a building?

Timeline

Looking at the financials, especially the capitalization rate, how long do you want to be involved with the investment? Are you more interested in a short-term investment to sell off within 3 – 5 years, or a longer term of 8 – 10+ years? Most real estate syndication deals last approximately 5-7 years.

Evaluating a Property

If a property matches your criteria, that doesn't necessarily mean it's a great investment. We'll go over how to evaluate every part of a multi-family investment deal in chapters 8, 9, and 10.

The most important thing about setting up your multi-family investment criteria is that everything is based on your personal needs. Your criteria are based around what you want to get out of the investment and how much risk you're willing to take at the time. If you're flexible, your criteria can be more flexible. If you're set on specifics, don't consider investments that don't meet those specifics.

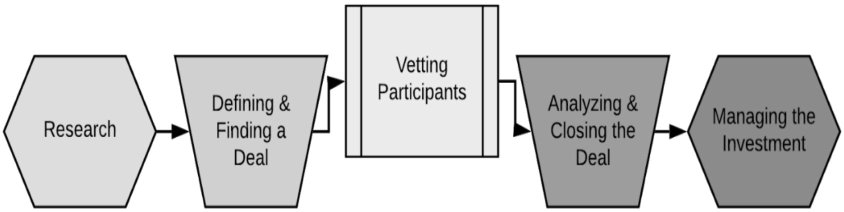
If you're not sure what you want to get out of an investment, or how those needs can be best met by a property, I'd love to help you sort it out. Head over to my site at MIRealEstate.us to read a few more resources or contact me:

- By Email - ismael.r@mirealestate.us
- On Facebook - @mirealestatellc
- On Twitter - @M_I_RealEstate
- On Instagram - mi_real_estate_llc

68

Chapter 8

Define & Vet the Sponsor



BLUF

1. Thoroughly vet individual and team sponsors
2. Look at: experience, reputation, preparedness, intended involvement
3. Your gut instincts will tell you a lot
4. No amount of vetting negates follow-up after investing

Vetting Is Your Responsibility

You're getting in on the deal and putting your money into the pot. If you haven't investigated the sponsor who's supposed to oversee asset performance, you're taking too big of a risk.

Being a passive investor is great. But you can't be passive throughout the deal unless you've put the work in to vet the deal ahead of time. When your money is with a sponsor you trust, you won't necessarily have to be as involved with the project as it progresses.

Multi-family syndication deals rely heavily on the sponsor. Even if it's a great deal in a solid market, you can still experience losses if the deal's sponsor isn't up to the task. Before you put any money into a deal, it's your responsibility to thoroughly vet the sponsor and make sure you're comfortable trusting them with the management of your investment.

Ideally, you need to find a sponsor who can protect your money over the long-term investment period, during any market conditions.

No one will do the vetting for you. If you don't look deep enough, or if you just don't investigate any of the other people involved at all, you're risking your investment and returns. Deals that go south could cost everything you've invested and may cause other non-monetary costs like reputation loss. If it's an equity deal, you'll be left with the equity you own in the property, which can be sold to recoup losses and return some of your money. If you're going in on a debt deal, (one where you likely get a higher fixed return, but don't have an equity position), you're at greater risk of losing your investment entirely.

Whether this is your first investment or one of many, always vet the sponsor for a multi-family syndication deal. It's a lesson you don't want to learn the hard way. All it means to vet the sponsor is to look closely at them, their experience, and their credibility to fulfill a deal like the one they're offering.

If you need to, you can outsource the vetting process. As long as you're presented with all the information you would normally have looked at yourself, you can hire out the process of searching for information if you don't have the time. Hire a trustworthy third party who has no connections with the sponsor.

There are a few specific areas you want to focus on when you're going to vet a project's sponsor. It doesn't matter if the sponsor is an individual or a company because the steps will remain basically the same. If it's a company, you may also want to take time to vet individuals in charge of the company.

Know the Sponsor

Your first step is always to know who you're working with. Sponsors can be individuals or companies. Either is fine, provided that the partnership is set up well, and the sponsor is a good fit.

It's important to know the people behind a sponsoring company. While it's easy to know an individual sponsor, sponsoring companies have a team of people working together on the project. You should know the people in the team, understand their roles, and be comfortable with the shared responsibilities of team members. The team itself should have a good reputation from past deals, or else the dominant individuals in charge should have that experience.

If one member is wearing too many hats or taking on too much responsibility, that's not a great sign for the deal. You want a diverse team with appropriate responsibilities for each person. Roles should be clearly assigned, and it should be obvious who is involved. Teams should be structured in a way that the deal can continue effectively, even if some of the team members quit or have been replaced.

Once you've defined your sponsor, you can move on to vetting them.

Experience Matters

Would you trust your investment money with someone who has absolutely nothing but an idea? That's a risky move you don't want with a syndication. Multi-family deals are high value. If a sponsor has no history of handling large amounts of money or even experience in real estate, it may not be worth getting involved. All things being equal, a deal with an inexperienced sponsor is riskier.

Personal Experience

Some sponsors have been working in the industry and sponsoring deals for decades. They have a great track record and are known by investors.

Other sponsors are newer to the game, even just starting out. They may not have a great track record yet, but that doesn’t mean they should be discounted right out of the gate.

Sponsors should have some experience to back up their proposal. Whether they’ve sponsored a deal before or not, they ought to have experience relevant to what they’re proposing to do. It could be experience working on a team with a sponsor, working in the real estate industry in some capacity, managing other high-value investments, or otherwise.

Team Experience

Companies that sponsor deals need to be vetted in the same way as individuals, including checking out the history of the main partners. If the company is newly formed, does it have partners with significant experience? Does the individual leading the team have years of relevant experience? Has at least one partner in the team been through a full market cycle?

Investment Strategies

How does the sponsor approach investments? Are they aggressive or conservative? The safest bet is an investor that approaches a deal with discipline and a sober mind. Ideally, they have a process already set up that they can explain to you.

A focused strategy is also safer than a scattered strategy. If they have a history of being involved in syndications or other real estate investments, do they stick to similar types, or are they all over the map? A sponsor that focuses on a particular real estate type, such as multi-family, is probably a more stable option than one that jumps around on different kinds of projects. Focused sponsors are more likely to turn a higher profit.

When a sponsor has a narrow project focus, you can count on them to having a bit more industry-specific knowledge to go along with it. Although different CRE types have similar characteristics, there are distinct differences in each sector. For instance, office buildings and multi-family have different tenant types and leasing strategies. Office buildings may require working closely with lease brokers to lock in 5-15-year leases, while multi-family units may be able to source tenants directly for 1-2-year leases in many areas. You want a sponsor familiar with the ins and out of multi-family, not just CRE in general.

Existing Portfolio

If the sponsor has assets they're managing right now or other investments they're involved with, it's good to look at those and ask some questions: What other assets do they currently have, and how are they performing in their markets? What's the return on existing portfolio assets?

Individual sponsors should still have enough room on their plate for the new proposed investment. When a sponsor has too much going on that they're directly involved in, you might want to make sure they can provide the attention necessary for your deal as well. Projects that are managed by someone other than the sponsor don't require as much direct attention on the day-to-day.

Contingency Plan

If everything goes wrong, how does the sponsor intend to make sure the investor's money is protected? This question is especially pertinent if it's an individual sponsor rather than a team. If something were to happen to the sponsor, what would happen to the deal and the money invested? Make sure the sponsor has a plan already. If not, it's something you'll want to discuss with them before signing anything.

Reputation

The overall reputation of a sponsor is one of the most important things to uncover. The safest sponsors have an excellent reputation that's free of questionable decision-making or incriminating evidence. Look into the reputation of any individual or company sponsor you're looking to work with.

Financial

Do what you can to find out about a sponsor's financial history. For a company, it should be easier than for an individual. Look for telling signs like bankruptcies, SEC violations, or criminal charges. If a bankruptcy or criminal case happened years ago and has a plausible explanation or served to teach the sponsor a lesson they've since corrected, proceed with caution. These two aren't necessarily deal breakers if nothing else seems wrong with the deal or the team.

SEC violations are trickier. Compliance is a huge issue in syndication deals. Non-compliance can bring about hefty fees and could result in legal trouble for the whole investment. You want to work with a sponsor that you're sure will work to be compliant. You don't want to have to follow up closely the entire time the investment is ongoing.

Industry

How is the sponsor's reputation in the real estate community? If they've worked on other projects with brokers, management teams, and other real estate entities, have they made a good impression? If the company is newer, find out about the reputations of each individual partner. Do they have a good reputation for honest work in the industry?

You want a sponsor to be honest, hardworking, and entirely dependable. If they fall short on any of these qualities, your investment gets a lot riskier.

Online

Social media and Google searches can help you uncover a bit more about an individual's or a company's history. While you don't need to dig deep, you should go far enough into the results to make sure nothing is incriminating there.

Read materials posted on LinkedIn and other social media, skim through books they've written, look briefly at their feed of posts. If anything stands out as particularly bad or makes you feel uncomfortable, you may want to listen to your gut instinct. Be aware of the timestamps on content and take that into account.

Investors

How well has the sponsor communicated with investors in the past? Do they have a reputation for keeping in touch and updating about important changes? Has it been easy for investors to get in touch with the sponsor?

Always ask a sponsor for Limited Partner (LP) references from past projects. If they can't provide you with any, that's a red flag. This only applies to sponsors who have previous experience, not to new sponsors. All sponsors with existing or past investor deals should be able to give you references. Use these references as a source for direct information about working with that sponsor.

If you're thinking about becoming an investor with a particular sponsor, you should know how they've worked with other investors before. This could be very telling for you.

Presentation

I can tell you without a doubt that how a sponsor presents themselves matters. Good presentation demonstrates preparation and some sense of commitment to doing well. If a sponsor can't be bothered to prepare for a deal with high-value investors before a project begins, they're not likely to be organized enough to handle a multi-family deal.

At one point, when I was looking at a new deal, I ran into a sponsor team like this. The deal was interesting and looked like it had potential. However, once I got in touch with the sponsors, it all went downhill from there.

When I was checking over the deal proposal they provided, there were numerous spelling and grammar errors throughout. This was the first red flag. Just like a resume, the sponsor should take time to edit their work and look for errors. Not a deal-breaker on its own, but a bad first impression.

The bigger problem was that the calculations for the investment deal were not correct. I did the underwriting myself, using the numbers they provided, and I could see they didn't do their math correctly.

Lastly, while participating in a videoconference to potential investors, the sponsor team seemed unsure about who was leading the meeting – at least that was my impression. There was no defined leadership. Defined leadership is crucial because you want to know who is in charge if something goes wrong. If no one can decide who has the final say, it means there's no clear guidance in difficult economic conditions or in case of unforeseen circumstances with the asset.

This was the sponsor's first time running a syndication. That's not a problem for me by itself. But, if you're looking at a first-time sponsor, presentation matters even more for them. After that chaotic meeting, I walked away from the deal and never looked back. I didn't feel like my investment was secure with the team, and I had no confidence in their abilities based on what I had witnessed.

Presentation isn't everything, but it's a huge part of creating trust with investors. Bad perception and a scattered image should be a red flag for potential investors. It's all about seeing how much care they put into their operations and how attentive they are to small details. When someone's done the work behind the scenes, it often shows. If they're not well prepared, that also shows.

Website

There's no reason a sponsor shouldn't have a website. It's a simple thing to set up that gives investors a way to learn more about the individual or team. A basic website presence is one of the first things you can easily look for from a sponsor.

Investment Package

A sponsor should be able to provide a packet of information about the investment upon request, usually after you've signed a non-disclosure agreement (NDA) to protect them. If they don't already have an investment packet available, that's a bad sign. It's the first thing you should be asking about when you contact them. Some sponsors might even have this freely available for anyone to download or view on their website, though it's not as likely for some types of investments, including 506(b) or 506(c), where investors have to meet specific standards.

As I mentioned before, the quality of writing and computations in the investment packet matters. Every mistake you find should lower your confidence in their ability to perform. Investment information packets should never look like they've just been thrown together at the last minute.

The biggest question their investment materials should be able to answer is how your money will be protected if you invest with them.

Sponsors who focus mainly on how much you can make without talking about how they plan to keep your investment safe, may not be the ones you want to work with. This is especially true of projects with a higher cap rate. If the sponsor is spending too much time talking about how much you could earn, without focusing on how they'll protect your investment in a higher risk deal, it means you'll need more information before moving forward.

Team Meetings

Sponsors should be well prepared for investor meetings. They should be able to answer relevant questions and give you some confidence that they'll handle your money well. You should be able to tell who's in charge of the team.

Deal Involvement & Management

How directly will the sponsor be involved in their project? Even if a management company will be hired for the building, the sponsor should be able to dedicate as much time as needed to the deal.

Full-time involvement is preferred, but not strictly necessary. If a sponsor's attention is divided between too many unrelated things, it can be an issue. Managing an investment property isn't just a part-time job they can fit into their existing schedule. Make sure the sponsor is able and willing to take on the responsibilities and time commitments the project needs.

If the sponsor is a property management company or works closely with a property management company, that gives a little more wiggle room for time commitments. They likely already have a sound system in place for managing investment properties and rentals. You can check out their existing projects and their current portfolio to get an idea of how they'll likely manage the new project.

Your Job's Not Done

Just because you vetted a sponsor and you trust them to perform well doesn't give you license to sit back and ignore your asset. You have to do some periodic asset management, even if you're not the landlord or caretaker in the deal. As a passive investor, your job becomes more of a supervisory role to make sure things are going along as they should.

Each month, quarter, or year, you should set aside time to review the financial reports and see what the sponsor has been doing to improve the NOI and keep cash flow consistent. Compare the financials with the proformas the sponsors prepared for you at the beginning of the financial period.

Visit your property once a year, if possible. Schedule it with the property manager and take a detailed look at the land and building to make sure what you're seeing on paper is what's happening on site. For tax purposes, one property visit per year is deductible.

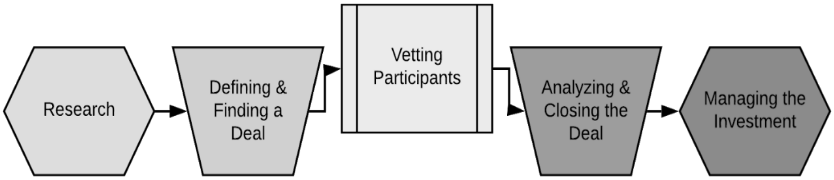
Vetting a sponsor thoroughly and really trusting them helps immensely. You won't feel quite as stressed about the deal or as nervous about your money, but you do still have to confirm that things are happening like they're supposed to.

We'll look into this a bit more in chapter 12. We'll also be looking into vetting your team and the deal itself in the coming chapters.

80

Chapter 9

Define & Vet the Investment Team



BLUF

1. Every member of the investment team should be vetted
2. Understand what each person involved does & their competence
3. Performing due diligence provides a high level of confidence in your investment

Who Is the Team?

As you may have gathered from chapter 2, there are more than a few people involved in a typical multi-family real estate syndication deal. The level of involvement for everyone varies, but many will be involved in some way over the lifetime of the investment.

If you want to be sure of the investment team, you need to perform your due diligence. This means vetting the whole team. You've already read about vetting the sponsor, which is one of the most critical steps, but you also need to look into the rest of the team. With so many moving pieces in the deal and plenty of contributing people or companies, it's a good idea to check them all out.

You'll vet each team member at a different level. The primary purpose of vetting the team is to make sure everyone you're working with has the relevant experience they need, understands the requirements of the project, and can perform their duties in a satisfactory way.

Vetting Legal Advisors

You'll have several legal advisors working with your multi-family investment team. A legal firm will probably be on retainer or else regularly consulted to work with the team on legal structuring, partner equity arrangements, dissolution, etc. They play an essential role in keeping your investment on the right path for legal compliance, so you have to pay attention to who you're working with.

Ask targeted questions to the legal advisory team, such as:

- How often do you work with real estate investors?
- What kind of real estate investment structures have you personally worked with?
- Have you set up real estate syndicates? Have you worked to close them out?
- What is your preferred legal structure for multi-family investors?
- How do you intend to keep investors protected under your preferred structure?

Vetting Brokers

When you're looking for a multi-family investment opportunity, it's common to work with a real estate broker to find a property. There's a lot of legwork that goes into finding an appropriate property. If you don't want to do the legwork, a broker eliminates it. The deal's sponsor may already be working with a broker, or they may have found the property for themselves.

Brokers are the first potential for loss in a deal, and you encounter them before the deal even begins. While brokerage fees are a one-time upfront expense that generally pays for itself over time, you could potentially lose a lot if you overpay for the building. Or, you could find a great deal. Part of that comes down to the broker you use and how good they are at their job.

Vetting a broker focuses on finding out how well they've done for other similar clients in the past. You'll want to ask questions like these:

- What type of properties do you focus on? (Ideally, multi-family)
- How many purchase escrows that you opened in the last year were successfully closed?
- What's the average above or below market price that your clients pay?
- What is the valuation trend in your market? (Over or underpricing properties)
- Are you working with the seller on this property purchase, or independently?
- How many investors have you worked with in the past, and do you work with any currently? (Get references if possible)
- Are you familiar with all available financing options in your area?
- How long have you been working in your current market?
- Does your state or local area have laws differentiating brokers and realtors?
- Can you tell me the reason why the property is on the market?

Vetting Tax Advisors

Sponsor teams may already have tax advisors on their staff or on retainer for them. You'll want tax advice before, during, and after the deal. A tax advisor needs to have experience dealing with every phase of real estate investment, so they can help you get the most out of the deal. Taxes are a huge part of investments, especially real estate investments, and they can cut into your bottom line severely if you don't know all about the laws and how they apply to your situation.

Work with tax advisors you can trust, who also understand the relevant local and national laws. If your sponsor has a tax advisory staff, you should also vet them. Work with trustworthy advisors or hire your own advisors if you don't trust those working with the sponsor.

Ask questions like these to tax advisors:

- Have you worked with multi-family investors before?
- How many years of experience do you have in real estate tax?
- What's your preferred tax strategy for investors?
- Have you worked with investors throughout every stage of a syndication?
- How will you keep me informed about new laws or tax code changes that affect my investment?

Vetting Compliance Officers

For significant investments, staying compliant with SEC and local regulations is essential. You don't want to be hit with legal troubles or enormous fines down the road. Compliance officers are an essential part of your team. Because they play such a large role in avoiding fees or legal issues, you want to make sure you're working with a compliance team that knows what they're doing.

Find out a bit more about them by asking questions like these:

- Have you worked with multi-family investors before?
- How many real estate syndications have you worked with in the past?
- Were you involved in the purchase, management, and sale of investment properties?
- How long have you worked in the market area you're in now? (Familiarization with local laws)
- What's your strategy for staying compliant from day 1?

- How involved will you be throughout the life of the investment? What does your involvement look like?
- What is your process for assessing compliance? Has it been effective in past investments?
- What experience do you have that's relevant to your current role?

Vetting Property Managers

If the sponsor is not going to be the property manager, or even if they are, you should be vetting the individual or firm responsible for managing the investment property. Property managers have the most prominent role in improving NOI for your investment property, so you should be sure they can do their job well before you allow them to work in that capacity.

When the sponsor is the property manager, you can vet them for their property management skills while you're also vetting their other qualities. If a separate property manager is going to be used, vet them once you know who's going to be doing the work.

Consider questions like these:

- What is the average NOI or NOL of properties you manage?
- Have you managed similar size properties in a similar class? How many?
- What's the average tenant turnover and occupancy in properties you've managed?
- How do you plan to grow the value of the investment property?
- How many turnkey properties have you managed vs. properties needing improvements?
- Do you have a strategic property management plan in place?

Vetting a Guarantor

For syndicated deals, guarantors are typically the borrower and anyone with more than 20% stake in the investment. The borrower may be an LLC formed by the investment partners. Whatever the case is, the guarantor(s) needs to provide information to confirm their ability to act in that capacity. The lender will require the information already, so you should check it out as well.

Typical information to vet a guarantor includes:

- Financial statements
- Credit records
- Cash flow statements
- A Resume or Biography

Depending on how the lending deal is set up, especially based on the down payment provided, a guarantor may not be necessary. Typically, in multi-family deals where more than 35% down payment is provided, guarantors are not requested by the lenders.

Why All the Work?

If you're thinking it sounds like a lot of work to vet the whole team, you're not wrong. To be a passive investor who doesn't have to step in much or be directly involved in every part of the process, you'll want to put in the work upfront. Working with people you trust to get the right things done is a huge advantage for you as the investor. If you can't trust your team, you're doing something wrong.

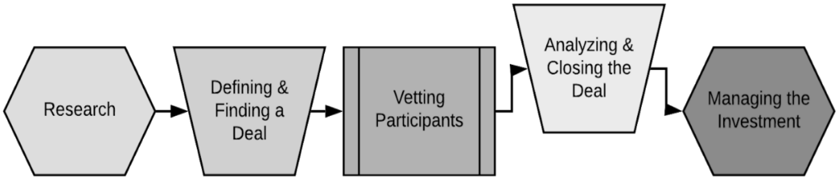
Having confidence in your whole team makes the entire investment smoother. If you're monitoring from afar and checking up occasionally, you can trust your team is doing things correctly. Without that strong sense of confidence that comes from looking into people yourself, it's harder to feel comfortable with their performance if you're not close to the deal.

In reality, you probably won't have to vet every team member in every deal you're involved in. You may work with the same trusted people repeatedly. But, just in case you need to, it's better to be prepared on how to check out every team member and what to look for. Why find a new broker if you're buying another property in the same area? Or, why look for a new tax advisor if you have high confidence in your existing advisor?

Multi-family investments are often a team effort. Do the legwork ahead of time to make sure you can trust your team before things go wrong. You want the best team you can get so you'll increase your chances of getting the desired ROI. If you run into problems in the deal, you'll be happy you took the time to vet your team thoroughly.

Chapter 10

Analyzing the Deal



BLUF

1. Due diligence helps you confirm information given by sponsors
2. Multi-family investments don't exist in a bubble – look at the market
3. Investigate the specific terms of the deal

What Does Due Diligence Look Like?

When you're presented with a deal, don't just take it at face value. If you accept the terms and decide to invest in the deal without confirming any of the information given, doing your own calculations, or putting effort into finding out more, you're not doing due diligence.

To perform due diligence and really examine the viability and profitability of a deal, you have to analyze the terms of the deal and all assets and liabilities involved. Whether you go in person to the property or not doesn't matter, as long as you've got the right sources and information to make confirmations.

Financial Structures

The meat of any syndication deal is the financials. There are a lot of things to consider here and a bit of legwork for you. You can't glaze over this part, because it's a large factor for determining if the deal has money-making potential or not. Don't go with your gut. Look at the financial structuring of the deal, especially these specific parts:

Projections

Every deal will present you with a collection of numbers, statistics, and projections related to the property. The numbers you're presented will generally be positioned to make the deal look as favorable as possible. Numbers don't lie, but they don't always tell the whole story, either. You need the context of where the numbers are coming from if you want an accurate picture of the pros and cons of the deal.

What you want to do is unravel the numbers and determine what the true projections should be. Take a close look at everything to check if the money-making potential of the deal is as good as it seems from the first look. If there's money to be made that satisfies your demands, it's probably a fine deal.

Fee Structure

Every deal will have some associated fees. These are a few of the most common ones:

- Asset Acquisition

When a multi-family asset is found and acquired, the sponsor or other entity that sourced and acquired the property is usually paid an asset acquisition fee. The average fee is around 2—4%.

- Asset Management

Whoever is managing the asset will get an asset management fee, whether it's the sponsor or a separate property management company. On average, asset management fees tend to be around 1—3 %.

- Asset Disposition

In some deals, the one responsible for selling the asset will receive a small fee for the service. This is paid for managing all aspects of the sale. An average fee for asset disposition is about 1%.

- Construction Fee

If construction is needed that will require rental to be delayed, the property manager may receive a small fee of around 1 – 2% of the construction cost. This is because the manager's payment usually comes out of rental income on a monthly basis, so the construction fee replaces that for the months that rent cannot be collected.

If other fees are tacked on, make sure you're paying attention to what they are and why they're being charged. Know what's normal so you can pick out fees that are higher than average or that are not normally there. Find out why the fees are high or why there are extra fees to determine if there will be a more substantial impact on your bottom line.

Project Budget (debt service coverage ratio)

For investors, it's recommended to pay attention to a project's debt service coverage ratio (DSCR). As discussed in Chapter 5, the DSCR refers to how much income is made for every dollar of debt on the property. You can find the DSCR by dividing the net operating income (NOI) or net operating loss (NOL) by the annual debt. An ideal ratio is at or above 1.25, but higher is better.

Low DSCRs make it difficult for you to qualify for a mortgage with the best terms. You need a DSCR of 1.25 or higher to qualify for some of the more competitive loans by Fannie Mae or Freddie Mac. It's not impossible to get a loan with a lower DSCR; it just may not be as good of a deal for you.

Profit waterfall

Some syndication deals have profit waterfalls. This is a system of determining how money is split and in what order of preference. With a waterfall plan, money is generally split in a certain way between sponsors and investors once a predetermined investment threshold is met. There is sometimes a hierarchy of money flow, but not always. For example, if a deal has a waterfall at returns in excess of a 17% annual rate of return (AAR), and the AAR is 21%, then a second set of pre-agreed upon return splits will dictate the distribution of that extra 4%. Some waterfalls I've seen split returns on 50/50% basis vs the usual 70/30% split.

Preferred returns

Plans that offer investors a preferred return provide that return before money is distributed elsewhere. It's a favorable deal for investors but not as favorable for sponsors. Some syndication deals will not offer preferred returns, choosing to put all investors on the same level as the sponsor.

Partner Roles

We've already talked about who the partners are and how to vet them individually, but you also need to look at how they're involved in the deal itself. Everything should be well outlined to let you know who's responsible for what, and how closely they'll be tied to the deal. Look at these things in particular:

- Are sponsors putting in their own money?

Sponsors (general partners) may not be putting up the bulk of the money for the deal, but having some skin in the game shows they have more incentive to do well. If they could incur losses from failure, you can trust that they'll act out of loss aversion, avoiding unnecessary risks, and finding useful ways to reach profits.

It also demonstrates that the sponsors see some potential in the deal as a good investment. If they're only looking for investment and aren't willing to put their own capital into the mix, it's harder to trust that they believe the deal is worth investing in.

- How are sponsors involved?

It's good to know exactly who is responsible for what. If things aren't arranged well, and it's unclear how many GPs there are or what their purpose is in the deal, that's not necessarily a good sign.

- How many sponsors and investors (limited partners)?

How many people will be splitting the pie? Who else is involved? While there aren't a lot of answers that could be deal breakers here, it's good to get some idea of the scale of the investment and the scope of people involved, both on the sponsor side and the investor side.

Market Comparison

It's worth repeating some of the key points in Chapter 7 - no property exists in a bubble. Even if a deal looks great, you need to consider it in the context of the market it's in. Keep in mind that while investment packages contain some market comparison numbers, these might be cherry-picked to show only the best numbers. Make comparisons for yourself if you want to be sure you're getting the full picture.

- Turnover

Once you know what the average turnover rate is for the property, find out how that compares to others in the area. You can determine average turnover in an area by asking brokers and property managers in the local area. If the property has a higher or lower turnover, you want to know why.

- Neighborhood

Does the property make sense in the neighborhood where it's located? Why do the sponsors like that particular neighborhood? Are there medical facilities, shopping facilities, and other necessities nearby? Look at the surroundings to see if the building blends in well with the neighborhood or if it has obvious flaws.

- Job growth

A higher potential for job growth in the area is a good sign for multi-family investment properties, especially if they are higher-paying jobs. Better jobs and higher employment rates tend to increase demand to live in an area, which will likely help keep demand for your property higher.

- Why this property over another?

Probably the most significant challenge a deal has is convincing you that this particular property is a better investment than any other. Once you've analyzed and investigated, you should be convinced that this particular property is a better place for your money than a building down the street or in the next county. If the deal doesn't leave you with that impression, it may not be worth considering.

Your money has a good chance of providing returns in other investments. If a deal offers a lower rate of return than you'd get from investments you're already doing, such as stocks or mutual funds, why would you want to add to your risk? Take the time to make sure an investment meets your standards and looks like a better deal than you'd get elsewhere. Multi-family offers you a good way to diversify with alternative investments, but that doesn't mean you should take the first deal on the table. Make sure your money is being put to good use.

Liabilities

There are so many liabilities to talk about with a building, but we'll just touch on some of the basics:

- Building age

Buildings can't last forever. Always look at the age of the building in question to see if it's worth investing in or not. Remember that syndication deals are likely to last for 5—10+ years, so consider that with the current building age.

- Necessary renovations/changes

Some buildings have a lot of positive characteristics, with some obvious flaws that need to be fixed before you'll make a good profit. Any necessary renovations and changes should be considered with the liabilities.

- Deferred maintenance

Has any necessary maintenance been put off that you'll have to pay for after purchase? Deferred maintenance should be considered in the building's valuation.

- Expenses

You want to have a wide margin of profitability once expenses are accounted for. Check the investment bundle to see what percentage they've placed expenses at. Even if that's the true number based on historical expenses, you might still want to overestimate expenses to around 50% to make sure you'd still be able to make money. Don't count loan expenses in your estimates.

Assets

As with liabilities, there are many specific assets that can be observed on a multi-family property. Here's an overview of some of the assets to look at on multi-family syndication deal:

- Cap Rate

The key metric for multi-family properties is the cap rate. The cap rate is inversely related to the property price, but directly related to the risk. Higher rate rates indicated a chance for higher profitability, but the deal is riskier. Lower cap rates usually indicate the opposite.

Don't just look at the cap rate of the property at purchase value. Compare it to the local market. Ideally, the cap rate should be a little higher than market averages, giving you a little more wiggle room to reach profitability in the deal. Conservative cap rates are better than anything on the extreme high or low side. Lower cap rates mean the property could be overpriced, while higher cap rates could indicate the deal is too risky for your purposes.

As a practical example, consider a few different classes of multi-family buildings. Class A buildings are usually low cap rate investments with little potential for income growth, but they're more stable and tend to have a higher price. In the middle might be a Class B building that offers some wiggle room for income growth, but it's also riskier than Class A and may not grow as anticipated. On the opposite end of the spectrum is an old, worn-down Class C building. The cap rate is sky high, along with the risk, driving down the purchase price. Cap rates don't always match building classes, but the general premise remains the same.

- NOI

What is the current and historical NOI for the property? Does it make enough to stay profitable on a monthly basis? You probably don't want a property with an NOL or a very low NOI, even if you think you can turn it around for higher rent or lower expenses. There are some cases where this risk might be warranted, but you'd need to look at a property closely to see if there's obvious potential to improve the NOI.

- Resale value

Is there enough demand on the property for you to get the full value back upon resale? Desirable properties can generally be sold for an appropriate value, whereas less desirable properties may have to be sold at a lower price than preferred. Properties with higher cap rates tend to have this problem, as they're too risky for the average investor to want to be involved.

- Property

The property itself is the biggest asset in the deal. Land value doesn't depreciate, so it's important to understand what the land itself is worth and how much of the overall value it accounts for. Land is also going to be a useful asset for resale, as the land may not lose its value over time, even if the building degrades and loses value.

Project Plan

A deal that's presented to you must have a plan for how the property will be managed, including cash flow projections. The plan should include:

- Exit strategy

What's the expected investment period? Syndication deals don't usually go beyond 7 – 10 years before resale. From the beginning, a good deal has an exit strategy that details how and when the sponsor plans to close out the investment.

- Financial plan

How much is projected to be made from the investment? Are the projections conservative or aggressive? Are all costs, potential expenses, renovations, and other considerations accounted for? Never enter a deal without solid financial information and projections.

- Cap rate

Capitalization rate was discussed in chapter 7, but it’s worth mentioning as part of the plan. Make sure the entry/exit cap rates make sense and don’t sound too good to be true or worse than you’d get elsewhere. Normally, it should be at least 50 (0.5%) basis points higher during your planned exit, for conservative underwriting.

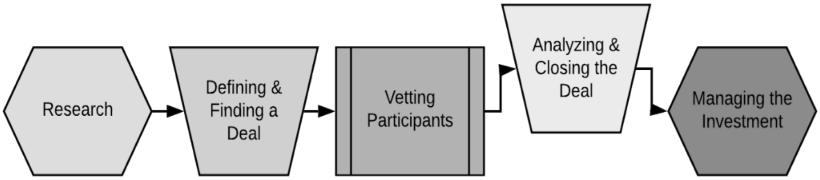
Selecting a Deal

The largest syndication investment firms in the US are so particular with deals that they may only accept about 1 in every 200 deals presented to them. If they’re so specific about the quality of the deal, why shouldn’t you be as well?

Spend time on due diligence, or outsource it to a trusted, useful third party that can summarize all the most important parts. It’s the only way you’ll know if something is worth your money or not. Match up the specifics of a deal with your criteria and investment preferences. If it doesn’t line up, it probably doesn’t belong in your portfolio.

Chapter 11

What Are Operating Agreements & PPMs?



BLUF

1. Paperwork holds up legally, pay attention to it
2. Seek out knowledgeable legal consultants
3. LLCs should have operating agreements
4. All syndicates should have PPMs

What's in the Paperwork?

Real estate syndications take a lot of upfront due diligence before any capital is turned over. A big part of that due diligence is going over paperwork presented by the syndicator (sponsor), namely the operating agreement (OA) and the private purchase memorandum (PPM). These two documents give definitions to each part of an investment team while also outlining the legal terms and conditions of the investment.

Operating Agreement

What Is It?

Operating agreements are documents that outline the roles and responsibilities of all the members involved in an LLC. For syndication deals, this includes both the sponsors and the investors, but does not include other support staff unless they have some ownership in the asset.

An operating agreement is the document that governs how things should be done in different circumstances and who is responsible for doing them. It will also make fee structures, voting rights, and ownership rights official while establishing the benefits and limitations.

When Do You Need It?

When a real estate syndication deal is set up with an LLC (which is the recommended legal entity for a syndication), an operating agreement is part of the initial setup.

A sponsor will create an operating agreement with his/her legal team from the very beginning, before the partnership is finalized, and the asset is purchased. If you're investing in a deal sponsored by someone else or an existing legal entity, you need to read through and thoroughly understand any existing operating agreements they have.

Specifics

Once you sign up to be a member of an LLC for a real estate syndication deal, you are bound by the contractual obligations of the operating agreement. Beyond the division of roles and responsibilities of each member, operating agreements also serve as a reference document to dictate what happens in certain predictable circumstances. These include:

- Death of a member
- Divorce between a member and their spouse
- Existing member exiting the LLC
- New member joining the LLC
- Member selling their equity stake to a third party
- Dissolution of the partnership
- Sale of the asset
- Business failure

- Lawsuits, mediation, arbitration, or legal altercations
- Profit divisions among members

Operating agreements are in place for legal protection of all the members. Even in one-member LLCs, an operating agreement is recommended to provide further proof of the legitimacy of the LLC and to show that it's not just a sole proprietorship.

Along with the special circumstances, operating agreements also define routine terms for the business, officially designate certain information as true, and label parties. You can expect to see these types of statements in an operating agreement:

- Legal name of the LLC
- Location and physical address of the LLC
- Meeting frequency and specifics
- Statement of governance under specific state laws
- Severance clauses
- Description of all LLC management
- Record of all capital and contributions, including additional investment, received from each party
- Liability placement
- Purpose and duration of the LLC
- Date of the LLC's formation
- Definition of terms and acronyms used in the document

Each operating agreement should be unique to their members and motives of that specific LLC. That's why it's important to review the document thoroughly, as it should hold all the information you need to know about how the deal will run and what level of involvement you'll have in it.

Member Voting

Membership in an LLC comes with complications around member rights and voting. By default, partners all have equal voting power for decision-making, but that can be modified by the operating agreement. Many LLCs will give the sponsor more voting power or near-exclusive decision-making power to speed up operations, simplify the role of investors, and protect the sponsor from being ejected from the deal. This is done by giving the sponsors more power in member votes by putting provisions into the operating agreements for the real estate syndication. It removes the burden for investors to be heavily involved in the deal, but it does put you at some risk if the sponsor begins making poor decisions that you and other investors disagree with.

Legal Considerations

Technically speaking, operating agreements are not strictly required in every state within the US. Some states do require them for every LLC, while others don't. Even if it's not a legal requirement to have an operating agreement, you shouldn't join an LLC that doesn't have one. This document is essential for clearing up any legal disputes that might happen down the road.

No matter how much you trust the sponsor, even if they're a relative or close friend of yours, an operating agreement gives you the legal protection to feel comfortable in a deal. If you don't have an official operating agreement, you could be subject to the state's default regulations for LLCs, which may not be favorable for any of the members.

Have your own personal legal advisor read through the operating agreement and summarize it for you so you understand your rights, obligations, ownership, and other factors completely. If an LLC doesn't have an operating agreement and you still want to invest in it, consider asking them to draft an operating agreement as a requirement for your investment capital.

If you're involved in drafting the operating agreement, don't settle for a stock agreement or pre-formed contract. Get your own legal representatives to draft the operating agreement for you. It's an essential document for resolving disputes and governing the roles of all parties involved. Considering your real estate syndication LLC will be handling large amounts of capital from multiple parties, investing in a strong operating agreement upfront will be worth it.

Private Placement Memorandum (PPM)

What Is It?

A private placement memorandum is a document released by a business offering private securities sales. It gives a detailed look at the company's finances, operations, and the investment they're offering.

This is not the same as marketing documents advertising an offering. PPMs are meant to be a thorough informational packet that gives a potential investor all the information they need to make an investment decision. It's factual and thorough and should not involve any marketing bias. Often, you'll have to sign an NDA before you can view a PPM.

When Do You Need It?

PPMs are created when companies want to offer investment securities that are not registered under SEC regulations. These securities can be offered privately if they meet certain exemptions. Real estate syndications can be offered privately because of Regulation D exemptions, but only if they meet the criteria of one of the categories.

PPMs are not necessary in publicly registered securities sales. But, considering most real estate syndication deals are set up under registration exemptions, you're likely to see PPMs associated with most of them.

Specifics

The purpose of a PPM is to give a detailed introduction to an investment opportunity with a private company. To this end, a PPM is likely to contain:

- Function and purpose of the business
- Source of revenues
- Intended duration of the investment
- Capital target
- Terms of the investment, including expected returns for investors
- Risks involved in the investment
- Summary of real estate assets to be purchased
- Plan of action for real estate asset
- Details of management team members
- Structure of the team
- Legal disclaimers, state and county-specific
- Description of securities
- Investor criteria

Included in these sections, you should get all the information you need to make a useful judgment about the property and the deal. If anything is missing from the PPM or if it doesn't address details thoroughly enough, contact the sponsor to ask more questions before making any further commitments.

There's no official structure or arrangement of a PPM, but they do tend to follow a similar format, and will often include a table of contents in the beginning to show you what they contain. They are required to give certain bits of information, which leads them to be formatted in a similar way to one another. Once you're familiar with the basic structure of a PPM, you'll understand how most of them are formatted.

However, unless you're the sponsor, you only need to be familiar with the basics. You are not going to be the one writing the document. That is the job of the SEC attorney. They are well versed in PPMs and know how to write them in a way that includes all the legal disclosures and information necessary to meet all regulatory standards. You should know what PPMs are, what their purpose is, and the basics of what they provide, but you're not going to be writing it for yourself.

PPM Examples

Most PPMs are only viewable after you sign a Non-Disclosure Agreement (NDA). For this reason, I can't share a PPM sample with you here. But if you do a quick search, you're likely to find free versions or templates available online that will give you a good idea of what to expect.

Legal Consultations

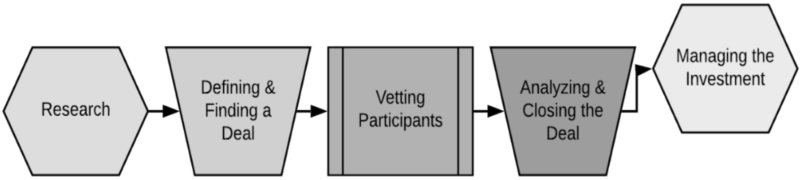
If you're going to be involved with drafting or reading an operating agreement or PPM, I would suggest seeking out your legal advisor's help. Work with a lawyer who understands and has experience with the documents you're dealing with. Just having them look the document over and help you understand anything that's unclear or interpreting some of the "legalese" that's put into these kinds of official documents can keep you out of a bad deal.

Everything that's promised about a deal should be in official writing. Don't rely on verbal contracts to form a binding agreement where your investment is concerned. Make it a prerequisite that official documents be drafted and reviewed before you invest anything in any project. Where those documents already exist, trust what's on paper over what's told to you in person, even if the sponsor assures you that a specific clause or statement will never be enforced.

What's in the paperwork is what holds up in court. Make the smart move and keep yourself protected by consulting with your own legal advisors instead of trusting your judgment or the word of a legal advisor affiliated with the sponsor.

Chapter 12

Property Purchased, Now What?



BLUF

1. Passive investors should track investment progress
2. Sponsors have day-to-day oversight responsibility
3. Initial setup is the hardest part

Multi-family Post-Purchase Responsibilities

Congratulations! You have your first property! Now what do you do?

This depends on your role in the purchase. If you're part of a real estate syndication, you're either a sponsor or an investor. As an investor, you're likely to have a very passive role.

Investors need to check on asset performance and stay connected to the numbers. At no point should you be clueless about how your asset is performing. You should always have some idea of what's going on, even if you don't have a hand in it or you don't know the exact numbers off the top of your head.

You're probably a passive investor because you didn't want an active role in managing the asset. This is understandable. It's very difficult to manage a multi-family asset while keeping up your day job and other life responsibilities at the same time. Passive investors pay a small management fee to the sponsor to avoid that balancing act.

Whether you're actively managing it or not, you do need to continue checking up on the asset regularly to track your investment and keep the manager accountable. Ideally, the sponsor is sending monthly performance updates during the initial 6-9 months, and quarterly once the property is stabilized. The periodicity of the updates should be addressed in the Operating Agreement.

Updates should include:

- Cash flow statements
- Income statement
- Balance sheet

Over the course of the deal, things may not always go as planned. If you're the investor, you should expect more communication if the deal is going poorly than if it's going well. Sponsors should be communicating more to keep you in the loop, update you on the progress for turning it around, and to demonstrate the steps they're taking to pull the investment back on track.

Sponsors have a lot more responsibility in a syndication deal. Some sponsors also act as the managers, giving them the daily upkeep duties alongside their existing responsibilities.

The sponsor has a direct set of responsibilities that fall under three main categories: asset management, financial management, and investor relations. Even if you're a passive investor, it's still good to understand what a sponsor will be doing with the property so you know how to keep track of progress accurately, and you can monitor the actions of the manager.

Construction & Renovation

Multi-family units are usually a good deal because there is some wiggle room to add value from the start. This will likely involve some simple renovations in a few or all the units or additional construction on the building. The building may need a full cosmetic upgrade, landscaping and outdoor revamps, simple fixes, or some new features in each unit.

Whatever the level of work that needs to be done, you should understand it before you buy the building. Now that you've bought it, the execution stage begins. This is where you'll bring in your team of experts to assess the situation thoroughly and formulate a plan about how to get things done. It could be as simple as a local company adding and replacing appliances, or as complex as a team of contractors doing full renovations or construction.

Whatever you're doing in this phase should have a direct impact on the value of the building by increasing income. The right improvements can justify an increase in rent prices while some additions might bring in extra income on their own, such as adding paid laundry facilities.

Do what makes sense for the property and the market area. If you overdo it, you could be wasting your money. If you don't do anything, you won't be adding value to the building and getting the most out of your investment.

Asset Management

From the moment you purchase a property, you take over the full management of it until the moment you sell it again.

While the asset is in your possession and under your management, you have a few goals to focus on:

1. Minimize carrying costs

During construction or larger renovations, there might be units that are uninhabitable because of the ongoing work. In this case, you're incurring costs that aren't being offset by unit income. Carrying costs are any asset-related costs that must be paid whether a unit is occupied or not. In other words, many of your operating expenses like taxes, utilities, and others will stay with you whether you're making money from tenants or not.

Minimize your carrying costs by working on a consistent schedule that's been set up from the beginning. Don't rush things getting done, but stay on top of any work to make sure it's on schedule and going as planned.

1. Reduce expenses

Often, the NOI of a property can be improved by something as simple as reducing monthly expenses for the property. Call utility companies and all service providers to negotiate better rates wherever there's wiggle room. Knocking down the monthly garbage bill or passing a fee on to tenants can improve your NOI.

Some expenses may seem concrete, but you may still have options to reduce them. For example, property taxes seem like they're set in stone. However, your building may be over-taxed based on an assessment that's higher than the actual taxable value. You can try to counter this by working with an assessor on your own and petitioning to have the taxable value of your building reduced, resulting in lower property taxes.

- Stabilize turnover

The main jobs of the property manager are to stabilize tenant turnover and keep as many units occupied as possible. Vacant units do not produce income. Management should take reasonable measures to hold onto existing tenants and to attract new ones as quickly as possible once a space is vacant. Reducing the turnover increases the occupancy rate on average, which has a positive effect on the building valuation as well.

Selling the Property

The culmination of a syndicated real estate deal is usually the sale of the asset. This generally happens within 5 – 10 years of purchasing the property. Ideally, the value of the asset will be higher than when you bought it initially.

Sales can lead to either capital gains or capital losses. There are tax implications for every investor who receives anything from the sale. Once the sale is complete, investors and sponsors are paid back their initial investment plus a share of the profits. The party involved in arranging and finalizing the sale will usually get a sale management fee before investments are paid back.

Refinancing Multi-family Properties

Rather than simply selling the property and walking away, many investors would rather refinance the property and reinvest the money into a new asset. A refinancing option gives investors the option to cash out or stay in for longer.

When you refinance, the hope is that you'll be able to borrow the same amount or more money than the initial investment. This allows you to move on to a bigger and better property and start the process over again without losing your equity stake. Make sure this option and the equity stake conditions are included in the Operating Agreement (OA) for the syndicate.

Wrapping Up the Deal

Once a deal is complete, everything needs to be officially wrapped up. This means closing the LLC, settling debts, and generally finishing up any outstanding processes. Your legal advisor can help you understand what needs to be done in your specific situation.

Whether you’re a sponsor or a passive investor, you have some role to play after a multi-family property is purchased. Do your part to keep the investment going successfully. Paying attention to how things are going also gives you the opportunity to interject if things aren't going the way they were stipulated in the Operating Agreement.

Setting up the deal is often the hardest part because of the due diligence involved and the initial time commitment upfront. The good news for investors is that setup is truly the most demanding part of the syndication process for you. Once that’s done and the deal is carrying on, you can continue with your normal life activities and just give attention to the deal occasionally. Stay in touch with the syndicate, but allow your real estate investment to grow as you focus on other areas in your life or passively investing in other properties.

Summary

From the outside looking in, every investment looks complex and perhaps frightening. Multi-family real estate syndication is no exception. Even the term itself seems a little intimidating. But everyone who's ever made money from a syndicate had to start somewhere. I had to jump for myself years ago, and I hope you now feel better prepared to do the same.

You don't have to know exactly what you're doing and make perfect decisions the first time around. If you pay attention to the most important steps, namely analyzing the deal and assessing the sponsor, you'll be able to prioritize these parts until you get a better handle on the whole process. Getting these high-priority steps right will make it hard for you to lose out from a personal error.

The market does what it will. No deal is free of risk. Keep your investment risks at a manageable level where you feel comfortable and don't let any sponsors or other investors bully you into a deal you don't feel good about. At the end of the day, this is your money, and you want to feel secure in where you've put it.

Multi-family investments can be a fantastic source of income for passive investors. Whether you're looking for a steady source of retirement income, a way to expand your portfolio or just an option with potential to beat the market average, multi-family is something you should consider. With the right team on your side, you can make it happen and start seeing the benefits for yourself!

About Ismael "Rey" Reyes

Rey has been actively investing in residential real estate since 2005 and has focused exclusively on multi-family since 2016. He has led MI Real Estate in investing in over 15 multi-family properties in Alabama, Florida and Tennessee, totaling in 1200+ units, valued at over $150 million US Dollars. Rey also provides independent consulting to multi-family investors and has authored several multi-family investing articles.

In 2019, Rey retired as Lieutenant Colonel from the US Army, with over 28 years of service, 23 of those on active duty. He first enlisted into the Army National Guard as a Military Police Officer. Later, he was commissioned as a Military Intelligence Officer, and then culminated his military career specializing as a Foreign Area Officer, responsible for providing Political-Military advice on Latin American Affairs to US military and civilian leadership.

Rey received an MBA from Columbia Southern University in 2010, is fluent in Spanish, and speaks some Portuguese. He is married to Mayerlyn Reyes and has two sons, Ismael (Junior) and Gabriel.

If you want to know more about passively investing in multi-family properties, reach out to Rey directly. He can give you advice and speak directly to your situation with more specifics and tailored comments so you can invest where it makes the most sense (#investwhereitmakescents). You can also check out his website, https://ismaelreyreyes.com/, or get in touch directly by:

- Schedule a Free 20 min call: https://ismaelreyreyes.com/20-mins-strategy-call/

- Email: rey@ismaelreyreyes.com

- Linktree: https://linktr.ee/IsmaelReyReyes