EPISODE 387

[INTRODUCTION]

[00:00:00] ANNOUNCER: Welcome to The Real Estate Syndication Show. Whether you are a seasoned investor or building a new real estate business, this is the show for you. Whitney Sewell talks to top experts in the business. Our goal is to help you master real estate syndication.

And now your host, Whitney Sewell.

[INTERVIEW]

[0:00:24.1] WS: This is your daily Real Estate Syndication show. I'm your host Whitney Sewell. Today, our guest is Omar Ruiz. Thanks for being on the show Omar.

[0:00:32.9] OR: Thank you very much Whitney, it's a pleasure to be here with you.

[0:00:35.3] WS: Yeah, happy to have you on the show Omar. Omar is the founder of LeRu Investments LLC with expertise in analyzing property financials and due diligence. Been a real estate investor since 2009, that started in property management in 2006. He and his partner realized how important property management was to successfully operating multifamily properties. They decided to start a property management company with a goal of owning larger apartment complexes. Since then, they've owned multifamily properties in three states and also flip properties in California and Houston Texas.

Omar, thank you again for your time and being willing to come on and share your expertise with myself and the listeners but you know, tell them a little bit more about how you got in the syndication business. You know, you and I were talking, you said, "We've been doing syndication since before we knew what syndication was." It's awesome, you know? Before it was called that, and so you know, give them a little bit more about how you got in the syndication business then I want to dive in, do your expertise specifically.

[0:01:36.7] OR: Okay, sure, well, I think like most investors, we started with smaller single family homes and it's funny because in the beginning, we really didn't know how to kind of put this partnership together, you know, is it a joint venture? Is it partnership, you know? We just didn't know which way to go about it, and the first deal we did which was actually with a relative, it just kind of made sense just to protect him and everybody else to just put our feelings on paper so to say and say, "Hey, this is what we're going to do, we're going to buy this. We're going to put the money for this."

And just kind of a quick one-page thing and told him you know, "We'll get it notarized." So then, you know, you have some sense of something being official I guess and if something goes awry, you know, you have a document that you can go to court and you know, fight for your rights. That's kind of really what I was trying to – well, what we were trying to do is, put some kind of document that would protect our partners or our investor's rights.

We were just raising small dollars, you know, 20,000 back then or 25,000 or 30,000. Smaller dollars but still you know, you still have to respect that and that was our main concern that you know – to protect people's rights, you know? To let them feel confident that their rights are being protected but as time went on and we learned about how to, you know – syndication was really actually we were doing, you know, we were just kind of doing it the wrong way because we didn't even know that that's what it was.

You know, we went to a couple of guys and eventually the – we hooked up with the right attorneys and got moving forward and luckily was at the right time in our business there.

[0:03:22.9] WS: Nice. Well, I'm glad you figured out the right way to do it and you're moving forward and thanks for sharing that very much, but you shared, even in your bio and then just me and you talking, just like your expertise of the due diligence process. I'd love for us to walk through a little bit of you know – maybe you give us an example of a recent deal you all have completed and then let's walk through the due diligence process that you took. You know, from the time you even found the deal, you know, to up to closing and then maybe even after.

Maybe give us an example of a recent deal and let's walk through that.

[0:03:55.8] OR: To me, there's two sides of the due diligence subject that you got the financial side and then you have the actual building physical property side of it. Both are very important. On the financial side, you know, when you're first looking at a deal, you have financial statements and the rent rules and other documented information that, you know, you're analyzing and putting your assumptions together to see if this is a deal, you know – what you're going to offer and be – and see if this is a good deal that you're going to go forward with. You're not actually able to do the due diligence on a lot of that stuff until after you get them to contract. That's really kind of where the rubber hits the road there.

Same thing on the building, the physical building due diligence. You can go visit a property, do a quick tour of it and look at the inside and kind of get an idea of what it's going to take for you to do, whatever improvements that you want to do or plans that you have in the future but, until you actually – once you get into the property and then you bring in other vendors.

For an example, it was actually a deal that I actually just recently had to walk away from. This deal had very sloppy financials on it. The property itself, I was okay with and I did bring inspectors to check the roofs. I had a plumber guy that came in and he scoped the lines on the plumbing there and that's when you know, you put a video. And one of the important things that came out of that is that he actually found roots in one of the main drain lines.

So, once we discovered that – okay, then we had to go back and kind of figure out okay, how are we going to overcome this? Are you guys gonna take care of that are not? There was a little bit of back and forth in that, but everything else checked out okay and then the other thing that came up is that they had the original windows there and this was out in Cincinnati so they get some pretty hefty winters out there.

There are windows and there are sliding glass doors were the old aluminum style and so those had to get redone so that played a factor in there. But the most important thing on that deal that forced me to walk away – the original financials that was provided to me by the broker were not sound officials. They weren't accurate and as we got into the deal, I had to really kind of pressed the broker and the ownership, especially on the utilities. They had a hard time getting the utility bills.

Eventually they did with a lot of poking and prodding and they didn't even know this but they actually had a couple of leaks in their water bill that was causing the water bill to be excessively. They had some utility issues there, but the main thing was, is that on their income side of the plate and on their expense side, you know, the income was not where they originally said it was. It was lower, and then the expenses were higher than what they originally did.

That's going to affect your return on investment there, and actually, Whitney, I was already in the process of talking to lenders on this deal, okay? I had actually approached like four different lenders on this deal. All of them were just having a tough time with the financials, you know?

[0:07:38.1] WS: The deal was under contract now or it wasn't?

[0:07:40.1] OR: It was under contract, yes, I have – we had earnest money, escrow and you know, this is – it's also why some people may ask, you know, "As a syndicator, why are you asking for fees or this and that?" Well, you know, I went to considerable expense, you know, hiring the inspector, the guy to scope the plumbing lines. I had a pest control guy out there and then I had a guy check out the heating systems in there. That all came out of my pocket. At this time, we hadn't even raised any money at this point.

Plus, I had to fly out. I'm in California, this was out in Cincinnati so I'm spending. I know I spent at least a week, maybe even two weeks out there. Obviously I got to stay somewhere. Those are all dollars that are coming out of my pocket, you know? I put my money upfront there but that was on the contract. We had earnest money in there. I was already done with the due diligence and now, was moving forward to the financing side of it and that's when I talked to all these lenders and they just couldn't get comfortable with the financials that were being provided on this deal.

I wasn't very comfortable myself at that point but you know, I wanted it to come from the lender so that then I can tell the seller, "Look, here's a situation, I can't even get financing on this deal, okay? It's because the financials that you're giving us are just not working."

[0:09:16.7] WS: I'd like to back up a little bit and ask you about how you started to discover this and I know you said the seller are as difficult to get some of the utility bills and things like that

and sometimes that's a red flag that either there's poor documentation processes that they have, they're not tracking those things, or else they're going to have that readily available, you know?

Or else, they don't really want to show it to you, right? You know, in this case, you know, how did you eventually get that information?

[0:09:42.7] OR: Okay, well, you're absolutely right about all those things you just said. Once we got out of the contract and I flew out there, I was able to really connect very well with the broker and the broker, you know, he enjoyed being there on the site, he accommodated me, and the guy was a total professional.

He liked you know, I was bringing all these guys in. The plumber guys, the H Vac guys, the pest control guys, the inspectors and then it was like clockwork. One, sometimes I had two guys on site. He knew we weren't messing around. You know, he wants to get his commission too, right? He wants the deal to close.

[0:10:19.3] WS: You're under contract at this point and you've already put money. Money's going hard, right?

[0:10:25.5] OR: We were still in the due diligence period. It was crazy, we actually extended the due diligence period I know at least twice and maybe even three times. It went for so long that we had several extensions and the seller was totally willing to extend it because they knew they were not performing on their rent and the story that I got eventually Whitney is that just prior to us going under contract, maybe about – maybe not even six months. Maybe about a six-month period prior, I guess they had this book keeper there that they fired because they weren't doing a good job and so they went through some staffing changes.

And in those changes, a lot of their financials and things just got really disorganized and the sellers, they're not – I wouldn't call – they weren't beginners by any stretch of the imagination but they were definitely not what I would call super organized and you know, on top their game. Minding the store so to say.

That's what was affecting them and so when they needed to gather up all this information, my god, it was like they were trying to look backwards to put it all together. I think this book keeper that they fired, I guess, did them a lot of disservice there and it seems like they got really loose with the delegation. They were't really minding the store so much.

[0:11:56.0] WS: What was the biggest reason you had to walk away. I know you mentioned the income was not where they stated or the expenses were also not where they stated but you know, was that the biggest thing or what else, I know you mentioned the windows and then even the leaks and things like that but was it just a combination or you know, was there something that said, "Okay, you know, any time this happens, we're walking away." Or, "This is going to cost too much to fix." What was it for you all?

[0:12:20.8] OR: The main thing was the expenses. Just the expenses were not going to make the deal work. I could, you know, see and project kind of forward, kind of where I could take the rents. That was fine, no issue there. But the expenses – once I got to real information on that stuff, it just was not going to make the returns, you know, to what we needed them to be.

That was the main thing, as far as the physical due diligence, I was okay with everything else. I knew we were going to have to raise some extra money for certain things but there were some programs that I was looking at – and that was the other thing that I discovered while I was over there. This was actually thanks to the brokers. There was a special program there where I would actually be able to do a special type of financing to do the improvements for the windows.

I would be able to amortize it out over many years. That was great but I was looking for a specific lender that can work within that program and there were a couple of them out there but the thing was that they just couldn't get comfortable with the financials that they were – they were just not up to snuff.

[0:13:27.6] WS: Okay, you know, are there checklists or anything you use specifically that help you know that you have looked at everything through the due diligence process that you need to?

[0:13:37.5] OR: Yes, actually, we do use a check list. We have a check list that we use ourselves and basically, it's a pretty involved checklist. It's several pages long but you know, it's got all the broker's information, all the different building mechanicals that we had to look through. The utility companies and all that stuff and yeah, the checklist, I mean, we use checklists for many things. Even for make readies, qualifying applicants. I mentioned to you before the show, you know, my background is in aerospace so we use a lot of checklists in aerospace.

[0:14:07.9] WS: I bet. So I know you all have properties in Cincinnati and Texas and you are flipping properties I think in California as well and you all are self-managing all of these properties is that right?

[0:14:20.3] OR: No, when we go – except for Houston because at Houston our partner is out there. But when we go out of state like I am right here in Indiana right now, we go with third party property management companies. We like to work more with the properties that have a CPM designation or the CCIM designation and it is a certain designation that you get after you have completed a certain amount of educational course work and you've had some on the job experience, and basically those are folks that are more career focused towards the management business.

[0:14:55.8] WS: Right, okay and so through the due diligence process, you know, how much are ya'll on site? You know, you're living in California. This property is more than half way across the country. So how often were you there? How much time did that take? You know, for people that are looking in other markets out of where they live, how much time were you having to spend there personally, or how time did you just have somebody else that is still in the ground there doing these things?

[0:15:20.9] OR: Yeah, I know on that last deal that I was just talking about, I know I was there for at least a week, maybe even two weeks, and sometimes what I like to do and maybe one of the nice things about the business here is that you do get familiar with a lot of different areas of the country. You know you're going to do a property tour or when you are doing due diligence, I mean, you get the opportunity to actually scout around different marks, I love doing that.

I love scouting different areas. I love seeing how the people live. How the communities are and I really enjoy that part of it but I am there every day to answer your question.

[0:16:05.3] WS: Okay. And then anything else in the due diligence process that you see that a lot of operators miss that you want to bring up to make sure that we know to look at these things?

[0:16:16.6] OR: Yeah, in fact early on, one of the biggest mistakes that I did – and this was back on the California deal. This was a property that we didn't verify rent deposits, okay? And so they were giving us a rent roll and these income statements saying, "Okay yeah, these tenants are paying." And everything looked okay. All right, fine. Well you know after we closed, we find out that like half of the people would not even paying but luckily it was a small deal.

It was only 13 units so once we knew what was going on, we just started just evicting people immediately but that is something that I would really caution people, I've actually talked to people that have had that same experience. Not verifying rental deposits. Now, sometimes that can be a challenge and on one of our best deals actually out in Houston, Texas, the seller – the way he ran his bank accounts, and I would not recommend that anybody do this, but, you know.

He had a construction company but he also owned several multifamily properties, but what he did is that he lumped all the income from all of his apartments into one single bank account. Yeah, so he had no way of separating up – and we weren't buying his whole portfolio. We were just buying this one property in this larger portfolio, and he had no way of separating that out of his bank statements of course, you know? So we had to rely on some of the deposit records that his on-site manager had.

And that we weren't super comfortable with that but you know at the end of the day you have to be – you know I remember an old mentor saying, you know, "Sometimes you have to make perfect decisions with imperfect information."

[0:18:06.1] WS: That is right and I am glad that you learned about the occupancy issue on a 13-unit not a 130-unit or a 200-unit, you know? And that is the difference in the economic occupancy and physical occupancy, right? That is why we have to know the income and – How

much should it be making? How much this is actually there, but like you said, when you get into financial statements and the previous sellers mixed it all in with something else that is difficult, right?

I mean like you said, you make the best decision with the information that you have, awesome. So going forward, how do you prevent that from happening?

[0:18:39.6] OR: Well you want to ask for bank statements, the way to do it, and if your bank statements, they match up, they may not match up perfectly with the PNL, you know, but as long as they are in line, you know, you don't see major diff – you know, you see a big $20-30,000 difference or something like that then you know something is up, okay? But bank statements are really the only way you can 100% verify that the income that is coming in is in fact that income.

Now, just so your listeners know, I have had it before where the seller was not comfortable with "Hey, I don't want people seeing my stuff," and all of this and that, and I said, "Okay, no problem. If you want, here is what we can do," and I went into his office. I said, "Look, I am just going to take pictures of your bank statement and what I will do is I will take a little sticky memo and I will put it right over the bank account number so nobody sees the bank account number and you don't have to worry about any nefarious activities." And he was all good with that.

[0:19:43.0] WS: Good, so Omar what is your buying criteria now? So you are talking to a broker and they say, "Okay what are you looking for or what is your buying criteria?" How do you answer that?

[0:19:51.4] OR: Well, we like to look at units that are at least 100 units and really the sweet spot is somewhere between 150 to 300 units. That is kinda the sweet spot there. We like to see that the unit mix is mostly two bedrooms. It seems to me that two bedroom units tend to stay leased up longer. That also depends on the market, you know. If you have a senior living community then that is different. You are going to want more than one bedrooms, and then if you are close to a university or college, then the one bedrooms might be better off for you.

But those are two of the main things and then we focus mostly on the B and C class stuff. The value-add stuff. If there is an issue with the management, we are pretty good at spotting those out. We do own a property management company in California so we are pretty good on what good sound management practices look like.

[0:20:51.6] WS: What's been the hardest part of the syndication journey for you?

[0:20:54.5] OR: The hardest part for me – well there's been a couple of things actually. I would say you have to put together the syndication and the properties and all of that stuff. The documentation. That to me wasn't the most challenging but I think what was is setting up the investors ahead of time before the deal is there, because if you do have the deal under contract then that is when you are starting to build those relationships with the investors.

You are going to be in a high anxiety zone and you are going to be moving very fast because you are also doing the due diligence at the same time, the inspections and all of that. So the best thing to do there is to start talking to your friends or families, your investors ahead of time of what your future plans are so that they already kind of know what you are doing and then communicating with them on a periodic basis I think is a good way to keeping them up to date.

[0:21:57.7] WS: And how are you prepared for a potential downturn that everybody's talking about?

[0:22:02.7] OR: Oh man that is a great question you know? And I tell a lot of newbie investors, really everybody in my opinion these are the times when we have to be very disciplined. It is very easy to want to get into a deal just because you see everybody else around you getting into deals and even kind of think maybe that Cincinnati deal kind of did that to me a little bit. It wasn't as big as I would like but I was very comfortable with the building itself.

But you know then in the end the numbers are the numbers and if the numbers don't work, the numbers are just not going to work and so in these kind of markets is very tricky to stay disciplined. I have been reading these books, I don't know if you have ever heard of Sam Zell. He's got a great book, I just finished it recently. *Am I Being Too Subtle*. It is a great book. Have you read that one?

[0:22:59.8] WS: I haven't but a lot of people have talked about that book. It is on my list.

[0:23:03.2] OR: Oh man that is a great book because it talks a lot about these kind of markets. You know, he is one of those guys who has been actually – he has gotten credit for being, I guess you could say kind of a prophetic in getting in and out of markets at the same time but he says in the book, sometimes he just got lucky, and then I am reading the book right now on Stephen Schwarzman. Do you know who that guy is? He is the main guy the founder of Blackstone.

I am just halfway into the book but that is a really great book that one of the heroes kind of guys, he helps me to be more disciplined in these kinds of times.

[0:23:37.9] WS: Yeah, so you are educating yourself. You are reading books of other people who seem to be ahead of us anyway, you know, understanding the market cycles, and what is a way – just a few quick questions before we ran out of time, but what is a way you're recently increasing deal flow?

[0:23:51.9] OR: Reaching out to brokers, and I am actually trying to figure out ways to reach out directly to land owners or landlords there by using public records to be in contact within effect. I have been trying to set up a system right now with the VA to help us do some of that work.

[0:24:13.9] WS: And what is a way that you've recently improved your business that we could apply to ours?

[0:24:17.9] OR: I definitely brought in – one thing that has helped me in the last couple of years was having an acquisitions guy to look at more deals for us and that has definitely increased the amount of offers that we have put out and luckily the guy, you know I give him a lot of credit. His name is Carlos Altamirano. He is out there doing this thing and I know he's got an Instagram out there but he is a really great underwriter and he has helped us out a lot in looking at deals and increasing our deal flow.

[0:24:47.4] WS: What's the one thing that has contributed to your success?

[0:24:50.0] OR: Having great teams around me and you know having good people on staff. You know if you have a bad egg on your staff there, you just got to get rid of those people as fast as you can, but definitely having good teams around me has always benefited us.

[0:25:07.3] WS: And before we have to go, tell us how you like to give back?

[0:25:10.5] OR: Oh well, a couple of ways. I do especially like teaching people financial education, some basic stuff. We host the Robert Kiyosaki game called – the board game called Cash Flow, so we host that over in our offices there in California every other week and that is a great way for people to get some fundamental financial information and then also kind of get to know us a little bit. There is also an event that the local people in Southern California Tennis called the 'I Survived Real Estate' event, and we have been a sponsor of that for several years.

And the proceeds from that go to help St. Jude's Children's Hospital and also to Make a Wish Foundation. We also house the largest real estate investing club in So Cal, it's called the Orange County Investment Club. So yeah, we have great speakers come out the first Tuesday of the month. We just had the guy, Joe Lahore actually the founder of the group. He was talking about mobile home investing and then next month I got a lady Asati Ashton that will be talking about vacation rentals. Short term rentals. Airbnb's.

[0:26:22.4] WS: All right Omar, well tell the listeners how they can get in touch with you and learn more about you?

[0:26:26.7] OR: The best way to learn more about us is on our website, it is called leruinvestments.com and it is spelled L-E-R-U, and followed by INVESTMENTS with an S at the end dot com and then you can also reach us at our offices. The number there is area code 888-682-2290.

[0:26:53.6] WS: Awesome, thank you, Omar.

[OUTRO]

[0:26:54.7] WS: Don't go yet, thank you for listening to today's episode. I would love it if you would go to iTunes right now and leave a rating and written review. I want to hear your feedback. It makes a big difference in getting the podcast out there. You can also go to the Real Estate Syndication Show on Facebook so you can connect with me and we can also receive feedback and your questions there that you want me to answer on the show.

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[END OF INTERVIEW]

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