

EPISODE 544

[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]

[0:00:24.3] WS: This is your daily Real Estate Syndication Show. I'm your host, Whitney Sewell. Today, our guest is Maureen Miles. Thanks for being on the show again, Maureen.

[0:00:33.4] MM: Hey, how are you doing, Whitney? Thank you for having me.

[0:00:36.5] WS: Yeah. My pleasure. My pleasure to have you back on the show. You should have just heard Maureen and her story and how she got into this business on the show WS537, just came out on April the 10th. If you didn't listen to that, I encourage you to go back and listen to her story there. Very encouraging and inspiring.

Also, a little about her, she started with renovating singles and duplexes and successfully made the transition to syndicating 100-plus unit complexes. She's also the founder and general partner of a property management company and construction company. She went from broke to 3,000 units after leaving her job six years ago, which you'll hear about in show 537.

Maureen, today I wanted to have you back and maybe you've done lots of deals. You had lots of success in multifamily syndication business. I'm honored to have you back and wanted to dive in just to how the process you have in developing a capital budget and just what that means, what that looks like when you're looking to purchase property and why don't we just dive right in.

[0:01:38.8] MM: Sure, sure. When we're looking at a potential deal, what we do is when we're underwriting the deal, we have a section for capital expenditures. Once we get the deal where we see it'll work, maybe we're looking at a little bit of rent increases or not, depending on the deal, but we'll have that capital expenditure sell that we will increase to see, "Okay, how much can we spend on this deal in order for the deal to work?" This is something maybe a little bit older, older properties you're going to need more capital, capex. Newer properties sometimes are a little bit tighter. You don't need so much, because there should be a newer property and run smoother.

What we do is we play around with that number and know that I can spend X amount and still be okay in this deal. By this time, I have a few ideas. I'll know if the rooms are shot. I'll know if I want to replace windows. I'll just have a really rough estimate of what I'm thinking we could spend, just shooting from the hip, or what I need to spend. Then we go ahead, we make sure that capital budget is there. That's in the very initial stages even before we put an LOI in, we're looking at those items.

[0:02:46.7] WS: At that point, while you've toured the property, I mean, you have an estimate, okay, it's this many units. By this time, I mean, you've done this enough, you know, "Okay, this potentially age of the property, or this potential type of property depending on what it is, we know that this is roughly what it costs on average." Then that's how you're coming up with that rough number in the very early stages.

[0:03:07.8] MM: Yeah. I might just on the quick tour that we do with the broker a couple of units. We haven't done the physical due diligence yet, but I think you can get a feel sometimes for what you're expecting. If you're told 50% have been renovated or none have been renovated since 1970, you're going to have a different number in mind there, things like how does the mail center look, how do the amenities look, the rooms, the windows, the doors. You have this ballpark on where there's going to be a large project capex-wise, or just something where you're just going to maybe be upgrading some interiors or things like that. On that initial walk, we'll know what the expectation of that is.

I know, if I say okay, this deal still works if I need to spend, say under \$800,000. I know that this deal will still work. Then I go through and I say, okay, well we need rooms, we need playground,

we need this, we need that. Where am I on my budget? Am I going to be okay with a net \$800,000? Do I feel I'm going to be okay within that range? If it's a yes, what we do is we take that to our due diligence.

When we go and do the physical due diligence, if there's anything we're questioning, if I don't know exactly what my pricing is going to be on rooms, if there's some asphalt or paving that needs to be done, things like mail centers, you can look at those prices up yourself. Anything you need a quote on, you want those people to meet you out there at the due diligence time and then get your quotes back within a few days. Look, we really need these quotes back.

You'll also know how are they turning the apartments, what conditions are the carpets in. They already do vinyl flooring throughout. That's where you really get to play around with that capital budget a little bit more to see. We recently had that where they've done probably about 80% of all the LVP flooring. That stuff is going to be good for a while. We don't need to have a big budget on turns. We know it's going to bring our turn cost down. Those are the things we go into that due diligence time. Again, we'll bring to make sure we're still within that range.

When we start doing due diligence, if the carpets are really shot and the cabinets are falling off the wall and need to be replaced, then if we're seeing foundation issues, or floors that are really uneven and wonky, maybe we didn't notice the roofs were shot and then when we went out to due diligence then we started seeing leaks or something. That could discount the deal right there on due diligent, or we may have to kill the deal if we see over – we need 2 million dollars for this property and we know the deal works at \$800,000 max. That could kill a deal.

If we're walking it and we say, "Wow, 200 grand is really all I need." The units are all mint and playground is there. I know I have this big cushion, so I know it's going to be an even juicier deal for everybody, because I'm not going to need that extra money.

Now one thing I do want to advise is no matter what, you do want to have a reserve budget, because you could run into things that you didn't anticipate, like a coronavirus, right? That's one thing. Just to have that working reserve. Now that's the more expensive capital you have, because you have the bank's portion, your finance capital. That's going to be your cheaper

money. When you raise when you're a syndicator and you raise money with investors, that's more expensive for you.

Typically we'll raise it outside of the normal deal. We'll have that money raised out when we close, we'll have that money sitting in the bank. It is expensive, but I call it our sleep at night money. We know if something happens that we didn't expect, maybe the water heaters all start going at once, or something you didn't anticipate, you have that extra sleep good at night money. You're not going to have to pull from other reserves, or you're not going to have to erode your operating income, because you do have that capital reserve there.

[0:06:49.0] WS: You're going to raise it from day one. That way, you're not having to – Because a lot of people will say, “Okay, I'm going to take so much per unit over a year,” or something like that and get that reserve budget. I'm not comfortable with that. I also want it from day one.

[0:07:02.5] MM: Right. Now the bank does make you put a reserve also, \$250 to \$300 typically per year per unit. You will have that reserve. Sometimes, I think especially when you're new, you forget that you have to actually pay for those items first and then you can go ahead and get that reserve money back. That money has to come from somewhere. If you're well-funded yourself, it may not be such a problem. If you're new into this and you're on a tight budget, a \$75,000 or a \$100,000 hit for something could really impact you. If you have to have that money out and it's going to be another couple weeks before it comes back.

You always want to have that just reserve capital money as a cushion there. We sell properties a lot and never touched some of those funds. Sometimes we've never touched quite a bit of those funds, which is good. It costs us a little more. Like I said, it's asleep at night money. It ensures that we're not going to get tripped up with anything that's a surprise. Maybe there's a big sprinkler issue.

We had one property we had to replace 600 and something sprinkler heads, because they had been recalled or something like that. It was a mess and it was expensive, but we had that money set aside. Just things like that that you don't always anticipate.

[0:08:14.6] WS: Are there any other times where it's like, some surprise has happened where you've had to use the reserve budget you weren't expecting to?

[0:08:21.7] MM: Some of the older properties, sometimes you'll get some underground issues and you can't always see that, where you're replacing some of the underground feeds for water lines, or sewer lines, or things like that. Those can get pricey as well, especially if you have to start going through parking lots and things like that. Sometimes your roofing, it's hard to tell how many layers. Sometimes we've been surprised on layers of roofing, where in most states you're only allowed to put two at the max.

I mean, we've choose one property. I think we found four layers on there. I mean, we had a roofing budget, but it went over because there was way more dispose – we had to dispose a bit more trash. I'm trying to think what else has tripped us up. Sometimes the turns are a little costlier in a different area. Right now, we're looking at bringing in house and flooring guys. I think we're actually going to hire them with a construction company just to do flooring, because in one of the markets we're in, the flooring is just ridiculous. The price is –

[0:09:18.0] WS: More with the labor side, you mean, that was ridiculous?

[0:09:20.5] MM: Yeah, the labor and just calling that third-party vendor for flooring, just ridiculous prices. I'm just tired of paying those. We could hire a couple people. They'd be really good. They'd be dedicated to our team. That's where you're having enough units in a market makes an impact too. I think last year, we picked up about 700 units in that market and we're looking at some more right now. We have another hundred plus under contract. That's where that scale comes in, because you can do things like that to save money.

[0:09:47.3] WS: You can keep a flooring guy busy.

[0:09:49.5] MM: Oh, yeah, yeah. You just hire them full-time, because what I'm paying these guys over – like I could buy the material myself. I can get a discount on the material. We had one large project where I was literally – I think I talked about that, the 200 down unit project. We literally had a tractor trailer come and unhook and they would take the empty tractor trailer away with them. They are leaving the tractor trailer on our property, because we were going through

so much carpeting, so much LVP. We actually were buying it directly from one of the flooring manufacturers. We saved a ton of money doing it that way and just hired the installers ourselves as hourly. That has helped save money on capital budget.

When you're doing geez, it's probably 200 units. I mean, that's 200,000 feet of flooring. I probably all needed flooring at that job too. It's just ways like that of trying to save money and understanding your costs too, knowing what you're paying for a certain amount of course. That that one tripped us up a little bit, because we're paying a little bit more than I had anticipated. I didn't realize the raise, but I'll fix it. It will be fixed soon.

[0:10:53.2] WS: We're developing this capital budget, what are some other ways you see people messing up, or not just really understanding that process well enough to be prepared to have the proper budget.

[0:11:02.7] MM: Yeah, I would say make sure you get three bids. I would not just rely on – Something I learned a little bit into it too is my property managers, they're great and they do the best job they can, but they're not construction experts. Sometimes the contractor you have will tell them something that isn't correct and sometimes they're questioning, “Is it done right? Well, he told me this.” They just don't know.

Just understanding the scope and letting your team at your property know that if anything goes outside of this to contact you, because sometimes they will get fed BS. I'll show up on site and know what has to be done, this has to be done. If I'm not there, or some of my construction team isn't watching that particular project, sometimes things change a little bit.

I would just say have the scope drawn out very well and that helps a lot. Also, getting three bids. If you're on a market where you know other multifamily people through networking, through masterminds, makes sure you ask them who they is. I've gotten roofers and things like that before when I'm new into a market. You can also go to people that supply the materials and things like that to find good relationships, but make sure you get three different bids, because you'll be surprised at how different some of those bids can come across.

Make sure you have an expert there. Make sure. If you don't – we all only all know so much, right? If we're not great at understanding paving and stuff, make sure you have somebody there that does, or somebody on your team, or a friend you can call. Make sure you confirm that those bids are right, because the last thing you want to do is spend \$60,000 or a \$100,000 on redoing something to find out that it wasn't done properly or the right way. It's worth paying a construction manager to come down and I know there's consultants out there that you can hire on what you can do. Make sure you have somebody else who have eyeballs. I just learned to not trust the GCs. I said that big job we had with the 200 down units. I went through four general contractors. You just always have to watch your money.

[0:13:05.2] WS: We went through four general contractors.

[0:13:07.7] MM: Did I tell you that story that was the birth of the instruction company, basically. That job, we fired four of them. I mean, it's when you fire a general contractor for a big job like that, it's rough and disruptive, because every one of them was a mess. We still did it. We didn't lose time. We always stayed on time, because I would jump down there. I remember one time, I didn't go home for almost three months. I was literally every day showing up there, because I couldn't trust my general contractor anymore. I had to make sure it was done right.

Yeah. We had about 10 people from Connecticut, because I used to do the rehabbing in Connecticut. At one point, I had the people that help me flip singles come down to work on these giant multifamily properties, because I could trust them and they knew what they were doing. Yeah, you just make it work. Figure out how to make it work.

[0:13:57.3] WS: Wow. You mentioned earlier, like something may happen, or maybe in the budget that you weren't planning for and it may kill the deal. Is there an example that that's happened, or maybe where you could explain when's that going to kill the deal and maybe with the process of that.

[0:14:11.3] MM: Well, that's basically what your due diligence is for, right? Are you going to uncover something that you didn't plan for? That is the one time when it's acceptable to re-trade. I don't you guys know what the re-trade is, but it's a thing that some people just do it as a game. They'll come in higher than everybody else to get the deal and then they re-trade every

single thing. We don't like to do that. I want broker to know I'm going to close the deal and not jerk around the seller or whatever, just to get it done.

One of the instances where we did do that was a termite issue. We went through one of the buildings. It was a early 70s product. I don't know if you know what a termite tunnel looks like, but it looks almost like a straw, like a mud straw basically going up. We saw them from the basement going up just in one building on this one side of the building. They looked old to me, because they weren't continuous. It looked like a piece of the head gotten knocked down. I was concerned, because at some point there were definitely termites here. Now my concern is I have to make sure that I have enough capital in case I go up in there and we start doing turns. You could look at it so much. You can feel is the floor spongy? Is there any issues? I didn't see a big pile of wood shavings down on the floor or something that would give me a concern as well for some wood insect.

I didn't see any signs. I just saw those. It looked there had been a repair, so I asked the seller about it and they're like, "No, we didn't have termites. There weren't termites." I called a termite company out there. They're telling me they found them in that building. The seller was swearing up and down that they never had issues with them. I saw the repairs. You don't know who to believe.

What I did is I just figured okay, worst case scenario, what is it going to cost me? If this is night – it was a brick building, so structurally on the exterior it should be okay, so I would have had to just mess with interior stuff, which really is just flooring, you have subfloor, you have studs, your sheetrock. I'm like, "What's the worst-case scenario?" I figured that for \$200,000 I could comfortably fix anything that I found there for what we couldn't see, because we could see a lot of it. Send somebody up in the attic, made sure the whole building wasn't full of it. If I ran and I said I was comfortable.

I think we were buying that deal for about 12 million bucks. I said, okay, for \$200,000 I'm good with it. I went back to the seller and I said, "Look, I can't definitely represent to my investors that there's no bugs here. I have to make sure that we have enough capital to cover it." I said, I'm literally going to walk from the deal – For the \$200,000 credit, we'll still continue with the deal. Otherwise, I'm walking.

I really was ready, so I don't bluff. I don't like to play games. We ended up getting the \$200,000 credit. Or actually, no. I want to do a cash payout, because you want the cash. You just don't want a credit on purchase price. We got that and that worked out. That was one of the reasons, or that was one of the times when I did re-trade and actually the only time I re-traded and it worked out. You have to be willing to walk, I think.

[0:17:12.5] WS: For sure. I'm sure he could see you were serious.

[0:17:15.5] MM: Oh, yeah. I was ready to kill the deal. There you are.

[0:17:19.3] WS: You just mentioned – something you could elaborate on right there. You said you wanted the cash versus the credit in the purchase price.

[0:17:26.2] MM: Yeah. If you're buying something for 12 million dollars, if your purchase price now gets changed to 11.8, is that really going to do anything for you? You want that cash in case that termite stuff is there. You want to have that cash. They will credit to usually towards your closing credits is how the money that you'd have to show up with that closing time, you want to make sure that the credit comes out right there. That'll help with – It'll net out, so that you actually have that cash at the end, because it's less you have to wire into the bank, or the title company at closing. That's the way you want to do it. You don't ever just want that reduction, because it's like a blip on the radar. You don't really ever get that money, if that makes sense. Yeah.

[0:18:13.7] WS: It does. For sure. Any other just final thoughts about developing that capital budget that you want to leave the listeners with, Maureen, before we run out of time?

[0:18:22.3] MM: I'd say just be really careful. Know what your insurance deductibles are, because you always want to have that handy in case that ever comes up. Know what your reserves are, even if you're doing – like right now, we are doing a bridge loan with in over 2 million dollar construction renovation loan in there.

You have to send that money out before you get it back. You want to make sure you have an extra \$500,000 that you can send out, come back, send out, come back, because that money does take a little while. That could really trip you up. If you're brand-new and you barely scraped together enough to close the deal and you don't have a lot of reserves, I mean, how are you going to spend 2 million dollars and wait for that money to come back? It would really trip you up. Just be aware of that.

Then raise enough too. Have somebody else look over your budget if you're not a 100% sure. That's where I see a lot of people getting tripped up. If they're going to get hurt in this is they don't have enough capital reserves. My first deal, I raised \$50,000. Somehow, we made it through that, but that was luck. I just didn't know any better. Luckily, I survived. I wouldn't do that deal again for \$50,000 capital.

[0:19:31.3] WS: Wow. Maureen, I can't thank you enough for your time and sharing your expertise and just how to develop a capital budget and some experiences you've had. Tell the listeners how they can get in touch with you and learn more about you.

[0:19:43.0] MM: Sure. Our website is www.4mrei. There's a contact us form. My e-mail is mmiles@4mrei. Yeah, just reach out if you have anything. I tell people, I'm always willing to help. Sometimes it's a little hard to catch me, but I'm always willing to help if you can grab me.

[END OF INTERVIEW]

[0:20:00.6] 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. Subscribe too, so you can get the latest episodes.

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[OUTRO]

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