EPISODE 1321

[INTRODUCTION]

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Brian Mitchell (BM): For the LP side, what you should look for from your general partner is determining who is handling the insurance. And, if you're able to get what they're going to buy prior to the closing of the property, if you're able to get the quote, do an analysis, understand what the square footage is of the property, and make sure that they're insuring it to value —really diving into the exclusions and asking some questions about it.

Whitney Sewell: As a passive investor, do you know what questions you should be asking the general partnership or the operator, the sponsor, all those terms, the guy that is leading the deal of that team, do you know what questions to ask to them about the type of insurance that they have. I bet that you are trying to mitigate your risks as much as possible when you're handling that operator or wiring your $15-150,000, whatever it may be, your hard-earned money, you wanna mitigate that risk as much as possible. And one way you're gonna do that is ensuring that the operator has the proper insurance. But, man, some of those things about insurance seem so complicated.

Our guest today is gonna help you, passive investor, to understand what questions you should be asking your operator or their team to ensure that they have proper insurance protecting your investment. Our guest is Brian Mitchell. He has been involved in real estate investing for about 4 years. He started with 5 units in 2018. He handled the property management for a couple of years and has seen purchased properties personally. He's traveling to masterminds, and real estate conferences, and he is an insurance advisor. I mean he knows insurance very well. And so, he's gonna help you today to be a better prepared passive investor to ensure that this team that you trust has the proper insurance.

[INTERVIEW]

WS: Brian, welcome to the show. You have the expertise that we all need on our team, to say the least. This is so important, whether you're on the active side of the passive side, you need to be knowledgeable about this part of the business.

Brian, welcome to the show. Get a start a little bit about our your expertise in the insurance field, kind of what you are doing, and then I want us to help advise you know some active investors, but also the passive investors how they should look at this part of the business when they are looking at a deal, but also as a passive when they're talking to a, you know, the general partnership or the operator as well, questions they should be asking? But so, who are you? Give us a little more detail.

BM: Yeah, Whitney, thanks for having me. Excited to be here and talk to you and hopefully provide some value to your audience. I'm Brian Mitchell. I'm an insurance broker up in Maine. We're licensed in all the States, and we write coverages for some real estate syndicators, and investors all throughout the country.

I'm an active investor on a smart port a small portfolio up here as well as a limited partner on 2 deals, one in Georgia, and one in Alabam. So I hit my twelfth year in the insurance business. Insurance can be a topic that would bore a lot of people. But I think if you can hang with us you'll get some good tidbits.

I come from the investor side, which I think is important because I can really see you know what the risks are, sitting in my seat right now, owning and managing my own portfolio, as well as being an investor, you know, as a limited partner. And I guess from the LP side, what you should look for from your general partners is to determine who is handling the insurance. And, if you're able to get what they're going to bind prior to the closing of the property, if you're able to get the quote, do an analysis, understand what the square footage is of the property, and make sure that they're ensuring it to value – really dive into the exclusions, and ask some questions about it because you're a limited partner, and you deserve to know what exclusions exist in the event there is a loss. Because if there's a loss, it's probably gonna come back to your return or lack thereof you know, to help cover those costs. So understand what they're about to put in place, and make sure the values are insured properly because we're looking at a market right now that is very interesting.

We're in an inflationary period and we have been for some time, so the cost to reconstruct these days are a lot higher than what it was 2 years ago. The cost of materials, Covid-related disruptions, labor shortages, and fuel increases, all that is pushing up the costs rebuild. So at the very minimum, make sure that the properties are being insured to full replacement cost value, look at the exclusions, and talk to your independent agent if you have any questions about how to interpret setting exclusions.

WS: Incredible. Well, we could about to stop right there. I was thinking, you know, as an LP, I've invested passively and the majority of almost all of our deals, and then, or all of them, I think, and then other operators as well. Asking for the insurance, I don't typically, probably enough detail around what kind of insurance they have on a project, you know when I am investing passively. And I mean we deal with that as an operator myself. And so I do understand some of that but I've not asked for that every time. But I should. was thinking about okay determine who's handling the insurance, get the insurance quote hopefully before closing and then make sure they're ensuring to value right and what exclusions exist, make sure values are insured properly, and you said to full replacement value.
But something that I even heard recently as well like even your home insurance, and in those things as much as values have gone up, and not so much the value of the property, but like what you said there, like the replacement value well, to build your home is gonna cost a lot more today than it did 2 years ago, much less 10 years ago, maybe when your home was built, or 20 years ago. And so you know it's like calling your insurance company, and like talking that through a little bit, right? Okay, we may have had a replacement cost 3 years ago but that's not replacement costs today.
Speak, to the passive investor. I may get that quote but I don't really know what I'm looking at. You know, especially when we think about the exclusions that exist or the replacement value. Well, how do I know those things to look for? Maybe good questions ask around those 2 things?

BM: Just understanding a little bit about the the the property that you're about to invest in. You know. go to the town assessor, page, and pull up the square footages are the buildings you're about to invest in, and then, you know, take a look at the insurance amount built into the

11:16:35 declaration section of the policy or the soon-to-be policy. So it would be the quote and just try to find out what your cost per square foot is.

And depending on the market, you know, in the southeast we're looking at about you know $135 to $150 a square foot. Up here in Maine, you can rebuild very little for under $200 a square foot. So depending on your market engage with a broker that has experience in, you know, writing in multiple states. If you have questions. you know certainly, as we all know, the benefit of being a limited partner is that it is hands-off. But it can be as hands-off as you want. I just think that you would be doing yourself good service by just taking a look at what they're about to put in place because it obviously needs to protect you as an investor as well.

And also, I'm a value-add investor as our quite a few people, probably listening right now. And depending on the value add a project, if it's a, you know, high vacancy situation or heavy lift where you know, days after closing, there'll be a full construction team, and you know renovating units, maybe kicking out some bad tenants and renovating those units. That will typically be an asset that's better suited for surplus lines carriers or ENS markets.

So those carriers are fantastic carriers to use in the event that you cannot get a standard company to write the insurance for the project at least the day of closing. And typically what I'm seeing some investors do is they're utilizing these ENS carriers to get coverage at the onset, but not looking at a standard market once the project is complete and the asset is put to its intended use and you're fully occupied. So the benefit of going to a standard market is the pricing is going to be a lot better than in the non-standard world. They're going to be far fewer exclusions and then there'll be some billing incentives where you can take advantage of a direct bill with the standard carrier versus a non-standard or ENS market.

You gotta write a checkout, one checkout it's an annual pay or premium finance. which carries a pretty high-interest rate. So, value-add investors, my suggestion would be to get that project completed, and once you do that look to other carriers because there could be some savings there, and most certainly a better product for you.

WS: Yeah, it's awesome. Brian, what you've see happening in the market moving forward? Anything that may be the active operator or even the LP should be thinking about? I know we've talked about a little bit of that. But anything else, as far as any predictions that you have moving forward or anything, we should be prepared for on the insurance front?

BM: Yeah, that's a great question. I mean prepare for more increases. We're in this hard market that we've been in since 2004, 2019. Catastrophic losses nationally and internationally have really pushed rates up for just about every carrier in every line of business. The cost to rebuild is manually pushing rates up because carriers are doing their own in-house replacement cost estimates. So they're no longer relying on old data that was in place when a policy was bound, say in 2017 or 2014.

You know your inflation guard is gonna bump up your property coverage, by 2, 4, 6, or 8% a year depending on what's in the policy and what the declaration page spells out for an inflation guard limit. So this hard market, no signs of slowing down. I think once things start getting under control from a loss perspective in this inflationary environment, sort of dies down a little bit, maybe we can see some potentially flatter or lower rates coming to us. But we're coming off a soft market at least since I've been in the business in 2010 up to 2019 when it turned into a hard market.

So no predictions yet as to when things are gonna change again. But I know we'll all be looking forward to that.

WS: No doubt about it. I appreciate that cause everybody wanna know like what's coming and all those things. Before we move on, is there anything else as you're even investing passively that you're asking an operator about the insurance that maybe we haven't talked about already?

BM: Yeah, I mean business interruption. Coverage is a big one. And I see a couple of policies here and there that come across my desk that I'm competing on that don't have the correct business interruption limit, or maybe they don't have it at all.

So many events of, say, a fire loss to your asset, tenants are going to be displaced because they can no longer live there. During this period of restoration, so typically 72 h after the loss, that's your deductible in business interruption, by the way, it's not a monetary deductible like it is in standard property coverages, it's an hourly deductible. And 72 hours is a common deductible. So 3 days after the loss, coverage will begin where tenants are displaced. You are no longer receiving the rental income that you otherwise would receive, had no loss occurred.

That coverage will stay in a place up to the policy limit or the period, or at the point that the period of restoration is over within the building is tenanted again. Whichever comes first.
So make sure you have proper business interruption limits are huge for the general partners and limited partners.

WS: How would we know what that limit should be?

BM: You would take a look at your gross rents, and then you would back out costs that you wouldn't be continuing after a loss like cleaning expenses, maybe certain landscaping expenses if those are discontinuing. So you back out those types of costs that would otherwise be their head no loss occurred. And that will get you a pretty good business interruption limit.

WS: It's good to know. Alright, so it's I was thinking about, you know, as a passive investor, knowing a few of these things to ask about, and I think it's gonna show you a lot about your operator. And I would also tell the LP, that not everyone on the team that you might talk to is going to be this knowledgeable about insurance right? There is going to be somebody on the team that's in charge. of making sure all these things are done properly. But you know, like even on our team, we have somebody that handles the insurance relationships. We have somebody that knows that part of the business in-depth and is ensuring these things are done properly. So they may talk to the investor, relations, person, and that person may not know all of these things about every one of our deals about the insurance specifically, you know.
But, we'll be able to get you that information, of course. So I wanted to just kind of flush that even more as far as passive investing, but even for the operator, anything else that they should be looking at right now as they're looking at deals or maybe specific markets or you know, you said to prepare for more increases, no doubt about it.
Maybe you can even help us there to think about what should we be preparing for, or even 2 years from now? Or you know as we're scaling out our underwriting, you know the 3 to 5 years, or even more? How do we plan for more increases in order to expect those and be as accurate as possible?

BM: A couple of years ago, I think we could put $500 a door for insurance, or $400 a door, and no matter what market you were in, I mean as long as it wasn't you know right on the coast it was pretty good, you know, number to use. But nowadays wow, I mean, there are, you know, $800 door, class 8, brand new construction deals that are being bound, right now in Dallas, Texas, and other large markets that are, you know, certainly well protected from fire with the fire departments and fire hydrants and sprinkler systems, and all of that. So it always figures a larger cost per door amount on your insurance, at least initially, while you're doing the napkin underwriting and engaging with you an insurance professional that has the markets.
Some of the smaller agencies may be really, really good to work with on your local hometown assets where they have local mutuals that some of the larger agencies just don't have access to. But if you're investing outside of your market it's specifically in different states, I would have an insurance professional on your side who has access to those markets, and who is license in all the States. That will suit you and your team very well. You could certainly use your guy on local stuff, and maybe pick his or her own brain on a deal that you got going on a few States over to see if they can help. But you know, make sure you're always utilizing somebody with some capacity, and experience in writing large property risks.

WS: Brian, that's very helpful. Yeah, you've just helped the active investor and the passive investor in many ways today. A few final questions. What are some of the most important metrics that you track?

BM: Cost per door is big because when I get a call from an investor who I've worked with a number of times, you know in there, underwriting a deal often the largest line item is going to be what is the insurance cost. And a lot of investors break it down by cost per door.
So developing cost per door and all the markets that we write in, and maybe markets that we're not writing in but my investors are looking at is huge. I'm, usually able to get a cost-per-door estimate off to my investors on the same day. And then obviously we'll have to underwrite it. But there are a lot of variables when it comes to underwriting, you know.
We gotta look at what the wiring situation is. If this was pre-1975, there's a lot of concern the carriers have related to aluminum wiring. We just bound a deal in January and a Mobile deal. I actually invest in it as well. It was 34 units with a $55,000 insurance price tag because of the

wiring. The wiring got remediated, and we were able to cut the insurance in half by going to a different market.

So try to get your insurance agent, you know, a real sort of high level as to what you know of the property, and they should be able to get you a good cost per door estimate, at least from the start. But, as we all know, it has to be underwritten. We gotta look under the hood and see what's there.

WS: Of course. What are some daily habits that you are disciplined about that have produced the highest return?

BM: Exercise. And that's something that I've taken more seriously as I get to my mid-late thirties, and it's a beautiful thing. Intermittent fasting is something I started sort of part-time a couple of years ago, which you can't really do part-time. So right now, but you know I take it more seriously you know, stop eating around 6 o'clock at night. Begin meeting again at 1130, noon the next day. The mental clarity is wonderful. The ability to get out of the house and not have to worry about eating anything is huge. You just get the kids ready, and then you're off to school. Reading more and allocating more time to podcasts. And meeting people and just becoming comfortable by being uncomfortable. Getting in front of people, and talking in front of people, are all the things that most of us really don't like to do, especially if we're slight introverts. Get out of your shell and just do it. It's not that hard. There's a lot of value to be had.

WS: That's incredible. I could relate to almost all those things you just said, and the exercise and the intermittent fasting, we've experienced a lot of good things from both of those things. But fasting is more of a newer thing for me personally, but it's been good.

What about the number one thing that's contributed to your success?

BM: Number one thing, you know, I think is the consistency. I have this fear of just being average in just you know, being locked into what we're all programmed to be locked into, which is, you know, get out of high school, go to college, you know, work to your 70, you know, save, rely on the market. You know I like side hustles. I enjoy it. I get a lot from it. The investing side of things is not easy. I had to put fire doors in a 4 unit that cost $8,000, and now

we just put $10,000 and fire escape balconies on a building that was built in 1890 and there's never been a history of fire.
And I'm thinking if the insurance company doesn't require this, and they're paying millions of dollars, or they have millions of dollars of coverage on this building why is the fire department acquiring it. You know, so it's trying to break the mold and not be average and not allow stuff like that to keep you from growing. And I think that's important because it people a lot of people can be dissuaded by doing more than the sort of quote-unquote have to be successful because of the red tape, because of the village review board meetings and all the things that you have to do. And you know, the taking on the risks, and maybe the risks of being sued for not doing something properly. I think you gotta push all that aside. develop a really good risk management program with your insurance agent and just enjoy the hustle and enjoy the journey.

WS: How do you like to give back?

BM: It's important for us to give back through our time. Our kids' school has a lot of initiatives in helping the community, and you know, with donations and stuff like that. So, we like to partake and do as much as we possibly can through the church as well as some monetary donations, as you know, as much as we possibly can.
So sort of relying on you know what their calendar of giving is a particular month. We definitely like to jump on as much as we possibly can and help the community.

WS: Awesome. Brian, I'm grateful to have had you on the show, and really to dive into some of the details around even what passive investors should be asking operators about insurance. I think that's very helpful as you are moving forward your hard-earned money, you know, to this operator, trusting their expertise and insurance, is such a big part of the deal, and just like minimizing a risk. And so it's so important and so I think you've provided some great values, especially for the passive investors around the front.
And so how can people get in touch with you and learn more about you?

BM: Yeah, I mean feel free to shoot me an email, brian.mitchell@crossagency.com. Happy to help, happy to talk real estate, happy talk insurance. I'm on LinkedIn as well. You know, on Facebook. Instagram, I'm trying to get a little bit more comfortable with. I haven't gotten there yet. So yeah, look me up. Let's chat. I'm involved in the, you know, few meetup groups, and you know, perhaps you know some of the meetup groups that you guys are part of, I'm already in. You know, I'm gonna be at the Jake and Gino Conference in November. And doing it a couple of other conferences before then. So yeah out and about for sure.

[END OF INTERVIEW]

[OUTRO]

Whitney Sewell: Thank you for being a loyal listener of the Real Estate Syndication Show, please subscribe and like the show, and share it with your friends so we can help them as well. Don't forget, to go to lifebridgecapital.com, where you can sign up and start investing in real estate today. Have a blessed day.

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