EPISODE 1465

[INTRODUCTION]

Andrew Brewer (AB): I focused a bit more on ground-up development. And what is typically meant by ground-up development is, you know, you're taking a property that is, you know, just the ground, and you are developing it by putting your development up by putting a building on it.

Whitney Sewell (WS): This is your daily real estate syndication show. I'm your host, Whitney Sewell. We're back again today with our guests, Andrew Brewers, many years and lots of experience in ground-up development. We're going to dive into different aspects of this asset class, whether you are active or passive. I know you're gonna learn a lot today.
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[INTERVIEW]

WS: Andrew, welcome back to the show honored to do a few segments with you and to dive into your expertise that you've honed in on in this ground-up development. I'm looking forward to learning more about that another listeners are as well as they heard yesterday more about your background and getting into this space. And that fortunate support you have at home around, you know, pushing into the just entrepreneurial drive that you and your wife have. So welcome back.

AB: Thanks for having me back.

WS: Let's jump into you know, ground up development like that. And I hear this term value add all the time. And let's talk about the difference between those two things a little bit for those that are maybe new or passive investors inactive as they're looking into these, they hear these

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these terms all the time, right? But what does that mean to you ground-up? And you know, what is ground-up, and then maybe what is value-add as well?

AB: Yeah, definitely. Value, it's kind of a blanket term. And of course, when you're doing ground-up development, you are adding value to the land. But usually, when most people refer to value-add, in terms of you know, commercial real estate, they're talking about adding value to an already existing property. So whether that's an office building, or an apartment building, or even just a house, they're somehow adding value, typically, that involves doing improvements on the property, you know, painting it, putting a new roof on, maybe redoing the interior is, you know, putting in new fixtures and stoves, and refrigerators and all that kind of stuff. And in theory than being able to raise the rents, which in turn increases the value of the property by increasing the net operating income or the NOI.

And that's an awesome way to do business. You know, and I've done it myself, I focused a bit more on ground-up development. And what is typically meant by ground-up development is, you know, you're taking a property that is, you know, just the ground, and you are developing it by putting your development up by putting a building on it, o that it is, you know, the land is now taller than it was before because there's a structure on it. And ground-up development, it can mean a number of different things. But the life cycle of a ground-up development project is somewhere in between, you know, what we would term raw land, which means, you know, land that has nothing on it at all, probably no utilities, no buildings, no structures, no zoning, or approvals or entitlements or anything on it, it's like just dirt.

And taking that through having a structure on it that is completed, that is being used for some kind of use, typically being leased or rented or owned by somebody, whether that's, you know, an apartment building where you have multiple tenants that are leasing the property, or you know, whether it's like an industrial building where you have like a big company, like, you know, Facebook, that puts a data center in it, and there's not really people there, but Facebook is leasing the space to essentially store and operate their equipment. Or maybe you sold the building to a company like Facebook, that still does the same thing. You know, they have their equipment in there, but they're not leasing it from somebody, they just own it. And there's

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multiple steps to that, to getting from point A raw land to point B of A final asset. And development can be, you know, anywhere in between that.

So there's multiple steps there, you know, typically you're going from step one is raw land. And from there, you get that raw land entitled, for what it is you want to put on that land. So entitlements will include things like rezoning making sure that there's proper access to utilities, or getting utility commitments from local municipalities or developing a plan to put your own private utilities on the land. And in doing that, essentially, you're approving that land with whatever the governing municipality is, whether that's a city, whether that's the county, whether that's the state, approving with them saying like, "This is what I want to do with the land, I want to put whatever this thing is on it." And they're saying, "Yes, we will allow you to do that as long as you come up with a plan that adheres to our laws."

So that's kind of step one. Step two would be, which would still be considered entitlement, which would be designing whatever that building or thing is, you know, and you have to design, you know, buildings or you know, whatever to adhere to, you know, local codes, and you have to fit within the frameworks that the city has said. So, the city may say, "Yes, we will allow you to put an apartment building there." Well, there's a question of how tall can that apartment building be? How many units can you have per acre of land? And all these kinds of things.

You know, and there will be a lot of different factors to take into account, you know, the city may say, "Okay, well zone, you say MF 20, which would stand for multifamily 20 units, so it'd be 20 multifamily units per acre of land." Now, maybe you've gotten approval, let's say you have 10 acres that you're trying to develop, and you've been approved for MF 20? Well, so you could put a maximum of 200 units on that piece of land. But in that the city may have a restriction that says, well, the buildings can't be over 40 feet high. Well, now you have to work in that the city may also or the city or county or whoever may also say, "Okay, well, for, you know, these units, if you have a two bedroom unit, you need to have two parking spaces per unit, you know, if you have, you know, one bedroom units, you need to have one and a half parking spaces per unit, or if you have three bedroom units, you have to have three parking

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spaces per unit." So now you got to figure out, "Okay, well, how much of my 10 acres do I have to set aside for parking?"

Because I have to have, like, I can't put you know, 200 units, if I can't have whatever it is, you know, 467 parking spaces, or whatever it is for your unit mix, you might also have utility constraints, you know, the city may say, hey, you know, we have water and sewer that goes to this area, but you know, really the capacity, it will only be adequate for, say 150 units, or, you know, however, many people that they would that fire code would say can live in those units.

You know, if you have a two bedroom apartment, you're generally not allowed to have 20 people living in that apartment unit, you know, the fire marshal will say like, "Hey, you can have a maximum of you know, two people per bedroom," which would mean a maximum of four people per two bedroom apartment unit.

So now if you have 200, you know, two bedroom apartment units, you're dealing with a certain amount of people. And you have to calculate that out with City's utility director of how much capacity do we have, there's all of these different things that you have to think about. And the end result may be, "Oh, well, although I'm zoned for 200 multifamily units, I can't actually fit that many units on this piece of land, because you know, I have to think about parking, or I don't have utility capacity, or my buildings can't be a certain height."

And, you know, for the passive investors out there listening, or even the newer developers, f somebody's trying to sell you a project where they say, you know, like, "Oh, yeah, you know, selling land that's entitled for, you know, 10 acres, it's entitled for 200 multifamily units," you got to be really careful. And it's like, "Okay, is it actually entitled, like full plans for 200 units? Or is it just zoned for that?" Because you don't want to go by a project and say, "Oh, I'm gonna buy this piece of land. And I'm gonna put 200 units on it. I'm gonna underwrite the deal." So that there's 200 units and based like a pro forma on that, only to buy the land and find out you can only get 120. That'll kill your deal.

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And you know, you'll be in a really tough, so everything has to be one story. Right? Exactly. So just a little tip out there for people looking at land and trying to get into development, make sure you know what you're looking at which I see a lot of people try to sell deals where they sell it that way.

WS: A couple of questions for you. When do you own the land versus when you're looking at the entitlements, getting entitlements, working with the city some of that? What's the process there of, you know, is that under contract to when you actually, you know, make an offer to compared to when you're actually ensuring those things, right, that it isn't titled properly or that you're actually getting an entitled.

AB: So everybody's a little bit different. People will close on the land at various points. Personally, in order for me to want to move forward with the deal, I like to know before I even go into the deal, how many units I'm going to be able to get, what my utility capacity is like. By the time I'm closing on a piece of land, I want to have a fully fleshed out business plan. And by the time I close on the land, the only thing that I have to do is basically follow a checklist, like, you know, my team and I will put together basically, like, this is our project schedule. And these are all of the tasks that we need to complete. And we're just essentially working through those.

We already know, for the most part, what the end result is going to be. Now we just actually, you know, have to do the work. Similar to you know, if you're starting a new business, while they're gonna make you form a business plan, you have to say, "I'm gonna, you know, take this step, and then this step, and this step, I'm gonna try to hit these numbers." And you know, you know what you have to do, but you still have to go out and do it. That's the point that I want to be at.

There is risk in development. I try to take as much of that out before I close on the land as possible. So typically, you know, I'll have a three to six month due diligence period, as well and negotiate for unless the seller has already done, you know, some of the due diligence for me, like I have a set number of things that I have to figure out before I feel comfortable moving forward.

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Sometimes I find property where the seller has already done some of that, you know, so for our 330 unit development that we're doing in Seguin, we bought the land from another developer, you know, what he had done is he had bought the land raw, and he had zoned it for multifamily. And then because he's a developer, he had actually gone through and figured out, you know, "Hey, these are, you know, the number of units that we could probably get this as the utility capacity." He had already done, you know, a waters of the US report, he'd done environmental report, you know, he'd run some of the third party reports for us. So we only had a 60-day due diligence period. But he already done essentially, what would for me had been two months worth of due diligence.

So I was like, "Okay, I'll take that deal, because you're giving me some of the information that I would need to find out." So it's a little dependent there. But you know, I'm always looking to, you know, figure out the same stuff on every deal. And it takes a while. You know, we have another deal right now, it's a townhome, deal 110 units that we'll be building up in Georgetown. I mean, we've been under contract since mid February on that deal. You know, we were working towards closing now. But you know, it's that was like a five month due diligence, you know, where we went through everything and develop that plan.

That's just how I like to do it. I know some people that will just go out and like buy the land. But you know, that's the riskiest way to do it in my opinion. I know a guy that did that out near Houston, he went and bought some land, and was like, "Yeah, I'm gonna develop this," and then went to the city. And they were like, yeah, and he was like, "Oh, well, well, that sucks." And, you know, other people out in the Texas Hill Country that bought a bunch of land, and they waiting to, you know, they're gonna put wells on it, because there's no water. And they went into the city. And we're like, yeah, so we're gonna, you know, subdivide this into, you know, whatever it is one to two acre lot and build houses on him. And they're like, "No, you're only going to subdivide it into like five to 10 acre parcels," and it blew their numbers. But they just bought the land, and they paid a premium for it. And so they're kind of in trouble now. Because they do that due diligence beforehand.

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And I think it's so important to do that, even if you lose money. And you know, and I have lost money and due diligence on deals. I've gone into deals, I've put up, you know, earnest money, you know, and lost. You know, I've lost my earnest money, I've lost my preliminary money that I spent on engineering and studies. And I mean, it's always better to lose that money up front than to go into a bad deal. You know, God forbid, bring investors into a deal, and then they're losing money.

Whenever I'm putting a deal together, you know, I go out and put the property under contract in my LLC name, I put up the earnest money out of my own pocket, I pay all the due diligence out of my own pocket, and I make sure that there's a deal before I start accepting anyone else's money on the deal.

WS: That's a good point, that's your process. Anyway, I think it's important for passive investors to know that but on that thought, what about some key factors, you would say passive investors need to consider this before, you know investing in a ground-up project or when they're evaluating it, or maybe even some of the risks associated with ground up that they need to be aware of?

AB: In my mind, everything is about your risk reward ratio, which differs per person, right? You know, some people have a little higher risk tolerance, they're willing to take more risk for less money, other people aren't. And so I always try to, you know, tailor my deals to take, you know, what I feel is an appropriate risk reward ratio into account. So there are certain parts of the development process that are a lot of risk. scarier than others.

For instance, trying to get land rezoned or zoned in the first place, is a lot riskier than working with land that is already out. So if you're going in, as a passive investor, you're going into a project and the sponsor saying, "Okay, well, we're buying this land raw, and we're gonna go, rezone it for whatever this thing is," that is a much riskier deal than someone coming in and saying, like, "I'm buying this land zoned for this thing, we're just going to put plans in place to build that thing, you know, the returns may be a little bit lower if the lands already zoned, but it's going to be a lot safer."

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You would think, by that logic, that buying a property where you already have plans in place is maybe an even safer deal, then that's not always the case, it depends. When those plans were put into place. If you're buying a project where plans were approved, like three years ago, haven't been built, they have the potential to hit a lot of issues there. And I had a deal, where I say that specifically because I had to deal with that happened, we bought a property, and it had plans in place already, you know, had full architectures and civil plans.

And, you know, we went in to start building, and the city came to us and said, "Oh, well, FEMA updated their flood maps. And now part of your land is in the floodplain, where it wasn't before when these plans were originally approved." And you know, FEMA is like God there, you know, like, you can't go against FEMA very easily. So they were like, you guys got to change your civil plans and account for more on site detention, like, sorry. And we were like, "Oh, well, that was never disclosed to us." And that's actually happened, like FEMA update the flood maps in between us closing on the land, and us going into start construction, which was like a four month gap. So it was like super bad timing there. We were able to figure that out. And you know, that kind of deal is still going well, it's just that could have that could have been a major issue there. So always be careful about who did the plans, and when they were done.

WS: A thought or just a question for a passive investor to ask a developer, right? Because if you've not been involved in any kind of development, you wouldn't know to ask that, I don't think. Any other quick questions for we have to move to another segment. Any other quick questions, or you would say, as a passive investor, you need to ask the developer this?

AB: I think you got to look at you got to look at the developers pro forma and see what they're putting in for their construction costs, and then go confirm that construction cost is feasible. Because a lot of people, a lot of developers that I know, they don't have the background that I have with actual like construction, and you know, budgeting expertise, you know, there's a lot of people that will, you know, call themselves developers, but really what they do is they just go out and like hire somebody to do it for them. And they're really just like a money guy, you know, they bring in money, and they go pay somebody to do it.

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And if they don't actually have knowledge of what it costs to build something, they may go and get a bid from general contractor who will lowball the bid in order to get the job. They think that the numbers accurate, but they're gonna get hit with a bunch of change orders later on down the project, which is going to blow the budget up.

So always make sure that you double check the the developers numbers that are on there pro forma, also make sure that you understand exactly where the project is like that is the number one most important thing is you have to understand what you are actually being presented as if somebody is saying like, it's a ground up development for this many units, it's like, that can mean so many things like are they entitled for that? Is the land already zoned? Is this actually feasible? You know, what do their numbers say? Those are all, you know, types of questions to ask, and then try to, you know, basically get a second opinion.

You know, you go to the doctor, you take your car, and whatever it is you go and get a second opinion, take that developer's pro forma, go bring it to somebody else, you know, I mean, if you bring it to another developer that's trying to get you into their deal, they may say a bunch of, you know, negative stuff about it. So always take everything with a grain of salt.

But you know, if somebody start, you know, if you take one developers pro forma and bring it to somebody else, and they go like, well, this doesn't sound right. Or they say, like, oh, well, this person said, this was a, you know, 200 unit development. Well, they don't even have the land zoned for that. They're just like, thinking that they're going to get it zoned for that. Well, then you got to look at the return and say, "Well, what returns are they offering me? Are they offering me like, a 15% annual return for a project that's going to require land to be rezoned?"

That's not an appropriate amount of reward for the risk you're taking on? You might want to see more like 25% returns with 30% returns for land rezone. And just you know, you got to understand the deal there. If you work with good sponsors that have, you know, good ethics, it's less of a problem. But you know, you don't always know how people are going to react in

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times of stress, you know, kind of unfortunate, everything sounds rosy at the very beginning, when it sounds like everyone's gonna make a lot.

WS: No, that's some good questions, some good thoughts for I think even active investors, right, you know, as they are approaching projects, or to be prepared for these questions. I knew I would want to know those things as a passive investor as well. If you're investing or when investing in a development, like say, get to know the sponsor, no doubt. I want to want to get to know them and then understand, "Hey, what's the likelihood of how they're going to perform in hard times?"

It's only a matter of time after like till there's some kind of deal that didn't work out the way you planned on right as an operator. I mean, it's just part of the business. You have to prepare for the unexpected, right or expect the unexpected. Andrew, I'm grateful for just talking through ground-up development in in detail, tell the listeners how they can get in touch with you and learn more about you before we move to another segment.

AB: So people can go to my website, which is www.irongallinvestments.com. That's my company. I founded it, I run it. All of my projects are through Iron Gall Investments. So you can learn a lot more about our projects about my team about myself and you know, my background through there. If you know if people want to get in touch with me directly, they can email me my email is andrew@irongallinvestments.com. You can also look me up on LinkedIn and Facebook. Not huge on social media right now. I guess I probably should do a little bit more self-promotion there. But, you can still find me there. If you want to, you know, connect there and send me a message or whatever it is. I'm always happy to chat with people make new connections and help out where I can. So let's get in touch with me and kind of go from there.

[END OF INTERVIEW]

[OUTRO]

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WS: Thank you for being with us again today. I hope that you have learned a lot from the show. Don't forget to like and subscribe. I hope you're telling your friends about The Real Estate Syndication Show and how they can also build wealth in real estate. You can also go to LifeBridgeCapital.com and start investing today.

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