



Multifamily University

MULTIFAMILY SYNDICATION DEEP DIVE

 How Investors Pool Money to Buy Large Assets

Our Goals for this Module



The Agenda

- Explain how groups of investors buy Multifamily properties together
- Talk about all the basics and key terms of a syndication
- To go through the Lifecycle of a Multifamily project
- Review



Syndication: Concept of Group Buying

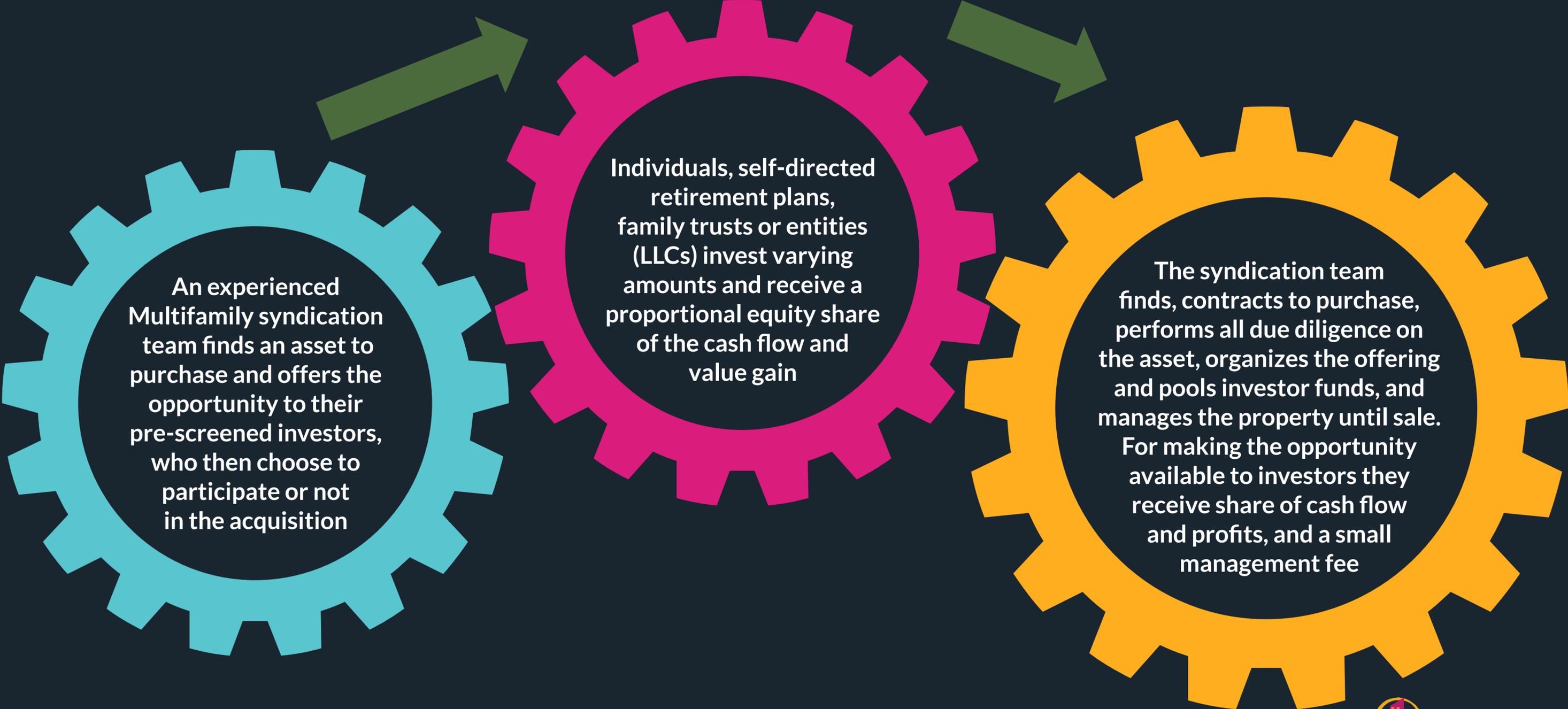


Multifamily complexes are expensive, so are commonly purchased by groups of investors using a mechanism called Syndication

If you want to become a syndicator, it's important for you to know that the rules of the Syndication process are governed by the SEC, for the protection of investors

The resource kit contains contact info of a strong Syndication attorney that can lead you through the process.

Syndication: How Does It Work?



Syndication: Governing Rules



Federal and state securities laws typically apply to real estate syndication transactions. Normally, securities may only be sold if the securities are registered with the SEC or otherwise exempt.

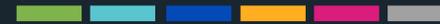
Traditionally, most real estate syndications have taken the form of a private placement exemption under Regulation D (Reg D).

Syndication: Governing Rules



Reg D has 2 commonly used exemptions, each of which requires the investors to be either an accredited investor or a sophisticated investor. Let us examine each type.

Offerings: 506(b) vs 506(c)



506B Offering

506C Offering

Communications with Investors

Companies may not advertise their security offering. Generally, companies may approach potential investors if there is a substantive, pre-existing relationship

General advertising permitted. Companies may advertise via social media, email, or offline. No substantive, pre-existing relationship with potential investors required

Eligible Investors

Accredited investors and up to 35 non-accredited investors who meet sophistication requirements

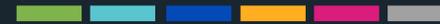
Only accredited investors

Accreditation Process

Self-certification via a questionnaire is the general standard

Companies must take reasonable steps to verify accredited investor status. Self-certification via a questionnaire is not permissible. The SEC issues examples of reasonable steps for verification

Offerings: 506(b) vs 506(c)



Accredited Investor

An individual that has made \$200,000 or more on an annual basis for the past two out of three years and is likely to make that same amount this year. If it is a couple qualifying together that amount is raised to \$300,000. If they do not meet the income requirements, they can qualify using a net worth of over \$1 million excluding their primary residence.



Sophisticated Investor

The SEC mentions sophisticated Investor as someone with enough financial and business knowledge to be capable of making an educated decision about an investment, although he may not meet the Accredited Investor requirements.

If the SEC were to ask why you thought this person was sophisticated you should be able to point to an internal set of standards so you can prove that caution was taken when making these decisions.

Management of the Property



Partner Types: GP vs LP vs Equity Partner vs Key Sponsor

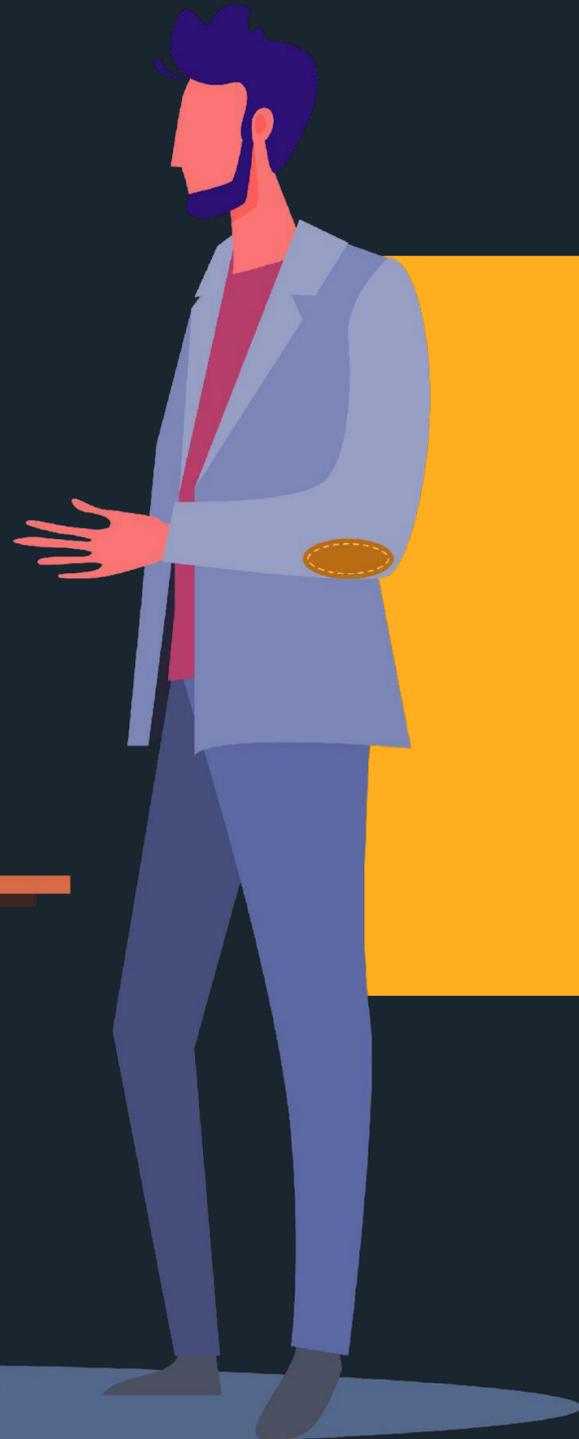


GENERAL PARTNER:

When a team of individuals work together to put a property under contract with the intention of managing that property, the members of that team are commonly referred to as General Partners. The GPs typically stay in the deal from beginning to end and receive a chunk of the profits. They are also often known as Promoters.



Partner Types: GP vs LP vs Equity Partner vs Key Sponsor



ASSET MANAGER:

The phrase is also often used to refer to GPs, though it has a slightly different meaning. The Asset Manager could be the same as the GP, could be a salaried employee, or could be a local partner.



Partner Types: GP vs LP vs Equity Partner vs Key Sponsor



EQUITY PARTNER:

As part of the GP team, their role and focus is to help raise money. Mostly, the equity partner helps the GP raise money, find investors, help to sign docs. Some equity partners also manage the investors and their tax docs for the entire duration of the project. Equity partners receive a chunk of the project, but there are strict restrictions on how their deal share can be structured. Examples are...

Partner Types: GP vs LP vs Equity Partner vs Key Sponsor



KEY SPONSOR OR PRINCIPAL:

A key sponsor or Principal is someone with a high net worth and a resume/track record of managing the type of asset being purchased.

Partner Types: GP vs LP vs Equity Partner vs Key Sponsor



KEY SPONSOR OR PRINCIPAL (CONT):

A key sponsor's net worth typically has to be at least as high as the loan amount on the property (other GPs net worth can also be used)

The key sponsor must have 10% loan amount liquid in bank account on the day of closing (other sponsor's liquidity can also be used).

For small properties, the GP (you or your team) can act as the key sponsor. For larger properties, you would need a key sponsor, and they would take a percentage of the deal for signing on the loan.

Partner Types: GP vs LP vs Equity Partner vs Key Sponsor



LIMITED PARTNER:

An LP or Limited Partner is the passive investor. While passive investors do not have any say in the running or disposition of the project, they typically provide most of the equity for the project.



Case Study: To Understand These Terms



John and Joe get together and put a 100 unit building in Boston under contract for \$5 Million

Limited Partner

John and Joe live in California so they ask Ken, a friend of theirs who lives in Boston to help to manage the property.

Equity Partner

Brad helps John and Joe raise the money for the down payment

General Partner

The down payment comes from Jason, Audrey and Keith

Asset Manager

The bank loan is for \$3.5 Million. John and Joe's net worth is not that high, so they bring in Ken to get them up to that mark

Key Sponsor or Principal

Typical Fees: Charged in a Syndication Project



ACQUISITION & REFINANCE FEES

Promoters commonly charge an acquisition fee for the property. Let's discuss typical acquisition fees. These fees are paid when the property is purchased, except the Refi fee, which is paid later.



ASSET MANAGEMENT FEES

Asset management fees of 1-2% of Effective Gross Income are quite common. Some syndicators charge 1% of the equity amount instead, which usually tends to be about twice the amount.



SHARE OF RENT PROFITS

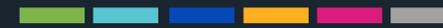
Promoters receive a percentage of the rent profits.



UPSIDE (PROFIT) ON SALE

At the sale of the asset, investors are repaid their initial investment 1st, then net profits (after accounting for investor capital, debt and selling costs) are commonly split between investors and Promoters in some ratio. If returns for the property are higher than a threshold, then returns ABOVE that threshold are split, but this time, the Promoters have a higher split.

Legal (LLC) Structure: What Does It Look Like?



Managers LLC

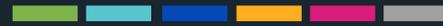
- Only GPs are part of this LLC
- GP splits disclosed in Op Agreement
- Higher liability
- Created in the state that property is

Investors LLC

- Asset lives here
- Managed by the Manager's LLC
- Lower liability
- LP/GP splits disclosed in Op Agreement
- Created in the state that property is in



Questions to Think About



How much money would you (as the General Partner or GP) need to put into the project yourself?

Does the equity partner invest his own money into the property?

Does the key sponsor invest his own money into the property?

What about due diligence, travel and legal expenses? Do they come out of acquisition fees?

Can you pay someone a fee to invest the Earnest Money?

Do the sponsors need to keep the liquid cash for the project in the bank for the entire duration of the project?



Lab Activity: How Much Do GPs Make?



Let's Figure Out the Amount of Money a General Partner Team Makes on a Typical Project

- The property purchase price is 10 million
- Total LP equity is 3 million
- Acquisition fees are 2%
- Gross rents are 1 million a year, and they go up by 2% a year
- Asset management fee is 1.5%. For simplicity assume that total asset management fees were \$75,000 over 5 years.
- Splits between limited partners and general partners are 70/30
- LP Investors received total cash flow of 1.2 million over 5 years.
- The project was sold after exactly 5 years, and the total profit after paying buying and selling costs and all fees was \$3.8 million.



Lab Activity: How Much Do GPs Make?



Let's Figure Out the Amount of Money a General Partner Team Makes on a Typical Project

- **Exercise 1:** Calculate total returns for General partners assuming THERE IS NO Pref for investors, just straight 70/30 split
- **Exercise 2:** Assume there were 3 general partners and each had 1/3rd of the GP pie. How much money did each GP make over 5 years on this one deal?
- **Exercise 3:** What was the Average Annualized Return for the LP investors.



Lab Activity: How Much Do GPs Make?



Let's Figure Out the Amount of Money a General Partner Team Makes on a Typical Project



- **Exercise 4:** What was the GP's Return-on-equity-raised. In other words, for every dollar that the syndicator raised, how many cents did the GP make?
- **Exercise 5:** For every dollar that the LPs made, how many cents did the GPs make? Was it 30 cents? Was it more?
- **Exercise 6:** If each LP investor invested \$100K, and the syndicator's marketing cost to find the investor was \$2,000, was this a good deal for the syndicator?



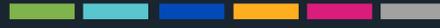
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LIFECYCLE OF A **MULTIFAMILY PROJECT**

Let's Walk Through an Entire Purchase to Sale Lifecycle

Phases: Multifamily Projects



Note that every Multifamily real estate project has a life and character of its own, but the goal is to understand the broad strokes of a Multifamily project lifecycle.

THE FOUR PHASES OF THE PROJECT

1

2

3

4

PRE-OFFER

1

PRE-OFFER



Metro Research: Jobs, path of progress, pricing trends



Team Creation: Realtors, Inspectors, Property managers, Contractors



Opportunity Search: Within target areas



Walk: Comparably sized properties for sale in target areas



Opportunity Found: First offer made based on seller's financials



2

POST
OFFER



Due Diligence #1: Roof, sewers, repairs, unit condition, carpets, hallways, exteriors, electrical, plumbing, mechanical



Due Diligence #2: Verification of financials, rents, occupancy levels, delinquency, staff competency



Due Diligence #3: Walk comparable properties on sale to ensure that our pricing and assumptions are sound, and the property is a good buy



Repair Credit Negotiated: Price reduction negotiated after financial verification. If seller does not agree, restart at Phase 1



Promote: Team promotes opportunity to investors, through webinars and detailed Investor Summary and financial projection documents



Legal Entity Creation: Lawyers create LLCs to protect investors and management. Purchase completed typically within 75 days, property handed over



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Retrain/Replace: Management makes changes to property management team



Upgrades: Management make upgrades to amenities, interiors and exterior to enhance satisfaction & curb appeal



Evictions: Management transitions out or evicts undesirable tenants, and brings in better tenants with higher rents



Repair Budget: Used to improve the asset, increasing rents , lowering expenses, and enhancing profitability



Distributions: Investors receive checks for available cash flow, and receive financials & a property report from the team



4



Operations: Management runs complex for 3-5 years. With market appreciation & better management, the property's income increases steadily



Exit: Typically, by Year 5 or before, the property's Net Operating income reaches the exit projections



Sale: Management puts property up for sale, and aims to complete the sale within a 6-month timeframe



Payment: Investors receive their principal back, along with profits



Questions: On This Module?

