

THE ULTIMATE GUIDE TO THE APARTMENT DEVELOPMENT PROCESS



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The Property Development Blueprint - How to Structure Your Projects -
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Preface

How do you complete a 100-mile race... The answer — a segment at a time, that's how. To think about it all at once is overwhelming. At 38 years old, I completed my first IRONMAN Triathlon. The IRONMAN was a difficult but very rewarding journey. I knew that I would do more IRONMAN races, but I did not expect that I would embark on another, possibly more difficult event. But after completing a couple more IRONMAN races, I set my sights on a 100-MILE RUNNING RACE. This would be four marathons back-to-back.

I had heard of athletes competing in ultra-marathons, but I had never considered it before then (then being 2006, 47 years old). I decided then and there I would, bearing significant equipment failure (this means my body not cooperating); I would complete a 100 MILER!

I have been running long distances since I was very young (about 8 years old) but had only completed marathons thus far. Since a participant must “qualify” for a 100 Miler (you need to complete at least a 50 Miler within a year of the 100 Mile event), I started looking for qualifying events. I found a 12-Hour Run in Texas. It was a 2.4-mile loop — around and around! See how many times you can do it in 12 hours. I increased my training to include more miles during the week and long runs on the weekends. After about six months of ramping up the miles, I ramped down for a couple of weeks before the qualifier. I was ready to go. I flew to Texas a couple of days before the event to inspect the location of the event (only to find out there was a 24-hour and a 48-hour race at the same time, they would end at the same time with the 12-hour race... I said to myself, “Whaaaat!”). I tried to concentrate on my race, not on the other longer races. One segment at a time. The 12-hour race (2007) went quite well. Oh, it was hard, but I managed to complete 63 miles. I had won my age group, and I was looking at the 100 Miler. I would target in 2008, the Arkansas Traveller 100.

I lowered my training miles for a while, then ramped them back up. The 100 Miler had rest stops every 4 miles and medical rest stops every 16 miles. I was putting in a lot of miles, the longest of which was a 40-mile run on the weekend. Most 100-Mile runs are quite hilly. The 12-hour run was pretty flat, so I didn't know what to expect of my “equipment.” The 100 Miler was in the fall of 2008. One of my brothers trained to join the race with me. About four weeks before the race, I developed an IT band pain (equipment failure?!). I nursed it and moved forward anyway. I was hopeful but

tentative at the race start (6am). At about 20 miles, my IT band started acting out, and by 44 miles, I was just about dragging the leg. So, that was that.... Or was it?

My brother hurt his ankle and had to stop at the 56-mile mark (okay, say it with me, “equipment failure”).

After about 2 days of self-pity, I thought to myself, “No way, I am going to recoup, fix the IT band and train again for next year.” After some treatment of the IT band and some rest, I was ramping up again. I realized there could be other equipment failures, but I wasn’t going to think about that. I set my sights on the same race a year later. That Arkansas Traveller is not going to get the best of me... It’s now Personal!

I was back at the race one year later. Stocked with some of the same clothing as last time and my headlamp (for the night-time running), I was on my way. This time, my brother did not have time to train for the race, but I was lucky to have my daughter (21) along as my support team. With no IT band issues and nothing else in my way, it was on. I was ready to concentrate on one SEGMENT AT A TIME. First, I would concentrate on 16-mile segments, then, when that seemed overwhelming, I would concentrate on 4-mile segments, and then, when my mind (and equipment) weakens, I would concentrate for 20 minutes at a time. Whatever it took. Besides the need to take a 10-minute nap at the 55-mile mark, and having to suck on salt rocks at about 60 miles to get my head and body right, I muscled through the 100 miles. Very few people can run the entire 100 miles. I ran about 85 of the miles and walked about 15 miles (a lot of steep uphill). Participants must complete the course in under 30 hours or they remove you from the course. I completed the course in 28 hours and 2 minutes! I really enjoyed the journey and loved completing my goal.

The above is ALSO a recipe for completing a successful REAL ESTATE DEVELOPMENT PROJECT. Like my training, it will take a couple of years to see a development project through. There will be setbacks and “equipment failures,” but stop, recoup, and find a path forward to complete the job successfully. And, just like my 100 Miler, a successful project requires lots of planning and execution.

So, go now and do your “100 miler,” whatever it is for you!

The Property Development Blueprint

Introduction

Who should read this book?

- Beginner developers
- Intermediate developers
- Subcontractors
- General contractors
- Construction loan officers
- Real estate investors

This book will not teach you how to pour concrete, how to frame, which air units to purchase or, generally, how to build an apartment complex; I am not an expert in construction. This book WILL help you understand the entire process of developing an apartment building (4 to 40 units), acquiring investors, buying land, entitling the property, planning the construction, securing construction and permanent loans, and stabilizing the rent roll.

I am a tax accountant with a degree in Mechanical Engineering. I outline in this book the various planning techniques needed during a development project, emphasizing the financial aspects of a project from a tax accountant's point of view. After you read this book, you will have learned about the entire development process. I paint a picture that allows you to talk to others in the construction development industry with a strong base knowledge of the development process.

There is something to be said for learning as much as you can about a subject before you dive into the action. This book is a great step toward gaining the proper perspective about how to approach apartment development. Remember, you do not need to know how to construct a building in order to successfully develop a property. As I discuss in this book, you need to surround yourself with knowledgeable team members in each of the disciplines required to complete your project. Financial team members, engineers, planners, general contractors and site supervisors,

subcontractors, city consultants, rental management, loan officers and, of course... a Tax Accountant.

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CHAPTER ONE

Develop by Design (Not by Default)

If you're reading this, it means that you've made a smart decision to develop instead of buy. The rewards for developing an apartment building can be much greater, so you're already on the right track.

But now, it's time to ask yourself one question:

How do I do it right?

And that's exactly what this book will teach you.

The thing is, nobody gets into development by happening upon a piece of land and starting a project. There's always planning involved.

But the problem is that there's not *enough* planning, or the project just isn't well-thought-out. Many developers get into it without a team, timeline, and many other considerations.

And this can be a major issue.

For instance, a client of ours wanted to develop a 30-unit building. But he'd failed to consider the timeline, which ended up being a costly mistake.

There was an argument between the client and an investor, after which the investor backed out in the middle of the project. This will likely be a set-back.

Luckily, the client was able to finish the project without going bankrupt. He even had decent success with it. But compared to what he could have achieved, the client undoubtedly failed.

All of these issues could've been easily avoided if attention was given to the items outlined in this book. Our mission is to ensure that developers check every single box when it comes to their projects, down to the finest details.

Bernstein Financial encourages developers to never go in blind. Before the project starts, they should have all the information they need to proactively deal with pitfalls and delays.

And with this book, we want to help you do the same.

No matter if you're a total beginner or an advanced builder, you'll find something of value in this book. You'll see exactly what it takes to complete successful projects, whether you're developing a 4-unit or a 40-unit apartment building.

Of course, it's always a good idea to start small when you're a beginner. Don't go out there and build a 30-unit building if you don't have any prior experience. The same mistakes you make with a 4-unit development will cost you many times more if you build larger buildings.

This is why we always recommend starting with simple projects and then working your way up.

You get to build up the much-needed experience and confidence to take on larger projects.

Besides, most banks require you to build a resume to mitigate the risk on their part. If banks see that you haven't built anything before, you might not get the financing you need. And even if you do, it may be on terms less favorable to the bottom line profit.

So, if you're new to the development game, don't rush it. Start small, and let yourself experience mistakes that you'll learn on a small scale and avoid in the future.

Naturally, our goal is to help you make as few mistakes as possible in the first place. By the end of this book, you'll see how to approach every project right and maximize your profits.

So, let's start with a fundamental rule that you must keep in mind.



CHAPTER TWO

Build Your Team (Because You Can't do it Alone)

One time, we worked with a client who wanted to buy a piece of land and start developing on it. His goal was to build a small apartment complex on the premises.

Prior to that, the client had only bought and sold properties. Because of that, he didn't know the ins and outs of property development. He felt like he was ready to buy and start building straight away.

However, we convinced him not to do so.

Why?

Because he didn't have anyone working with him. The client hadn't consulted an architect, developer, general contractor, and other vital team members.

We explained that there was no way of knowing if the land was right for him. Maybe he wouldn't be able to build what he wanted; the seller almost definitely wouldn't tell him that this was the case.

For this reason, we encouraged the client to take it slower instead of jumping into the purchase. We emphasized the importance of having all the right people by his side before he thought about the project.

Luckily, the client listened to us. He backed out of the deal and decided to gather a team of professionals first. He realized that he could end up with something that didn't meet his needs, and so he felt like he should take a step back.

This was a good call, as every developer must surround themselves with a capable team before they start building. Otherwise, you might expose yourself to a myriad of risks down the line. And your projects are far too expensive to risk your resources.

In this chapter, you'll see why and how to find the right people for your projects. We'll also discuss some of the details that developers usually don't focus on enough. So, without further ado, let's go over the list of people you need to complete a successful project.

The Professionals You Need to Work With

Generally, only the largest development companies have lots of employees who take care of every single aspect of the project. But for anything other than those large companies, there's no reason to have that many people directly under you.

Rather, you'll have some administrative staff, and you'll subcontract with various vendors and consultants required to design and build the project. This includes, but is not limited to:

- Architect
- Soils Experts
- General Contractor
- Site Supervisors
- Plumbing
- Framing
- Drywalling
- Electrical work, etc.

Now, you'll hire all those subcontractors and they'll be a part of your core team. You'll probably have many subcontractors, as well as the people who may manage them. This can be a general contractor or project manager.

Of course, you'll also work with engineers and architects that will cover the design and engineering work. In most cases, these will be cookie-cutter designs, as your architect has likely already worked on similar projects.

As such, these drawings aren't hard to produce for experienced architects, and they'll cost you between \$3,000 and \$10,000 per door (apartment unit).

And finally, you'll have your legal and accounting teams. You need to find the right people for the job if you want everything to go as smoothly as possible.

In most cases, this is what your core team will consist of. You might also have other team members that will expedite the process or handle the finances. But, for the most part the above team members are those that you absolutely must have in your core team. So, make sure you don't start a project before you've hired them.

Should You be the General Contractor of the Project?

When you start developing, you have two options. You can either be an investor and hire a general contractor that will obtain and manage all the subcontractors you need. Or you can be the general contractor if you have a license. Or you may build the project as an owner-builder under certain circumstances.

Bear in mind that if you hire all the subcontractors yourself, you're a general contractor by default. And this comes with a set of challenges that you need to be aware of.

Being a general contractor comes with many liabilities. There's also a lot of IRS reporting involved, which can be quite time-consuming and stressful if you're not 100% sure of what you're doing.

Because of this, there's a rule of thumb that you should never start out as a general contractor. If you don't have enough experience, you might create many headaches for yourself and make a lot of mistakes.

So, the best thing to do if you're a beginner is to start out as an investor. And then, once you've gathered enough knowledge and experience, you can get a license and become a general contractor.

When you eventually act as your own general contractor, you save money in the form of a general contractor's fee. You can eliminate that expense and improve profits.

The Tasks to Outsource

Even if you decide to become a general contractor, you'd want to outsource the majority of the remaining work. Even the best contractors out there can't replace many functions that you need, and you shouldn't try to do them yourself.

For instance, you can utilize an expeditor who will usually be familiar with city process, codes and zoning to ensure that your project can get off the ground. A consultant will know what permits you need and help you get them. If you don't have someone like that on your team, you might get into considerable trouble right off the bat.

One time, a client of mine got asked to be a consultant for another developer. The developer bought a piece of land with an old historic building that they wanted to demolish. It wasn't until after they'd done it that they realized this required approval from the city. The consultant coached the developer on their options to correct the problem.

While the project got back on track, it took around six months for this to happen. As you can imagine, this was a huge delay that cost the developer a lot of time and money.

To avoid making this mistake, follow the general rule of knowing that if you are new to a situation, get help. Stick to your expertise, and outsource pretty much everything else to the right people.

Planning is Crucial

Property development is a complex process. There are many moving parts to figure out before you can confidently start building. This is why you need an airtight plan before you start developing.

Besides, if you need to bring in other investors, they'll want to make sure that the project is financially worth their while. For this reason, you need accurate financial projections and a detailed development plan.

Now, there will be times when investors won't see a large return right away. Profits might be slim at the beginning, but they'll grow as the value goes up. And historically, this has pretty much always been the case.

With that said, you can't rely on external forces and merely hope for the best. Instead, you need to perform your due diligence and generate a feasibility study. You must know what's possible for your project and be 100% certain that you can complete it successfully.

You need to be conservative when making all projections. Factor in any possible delays and negative expectations that will show the investors that they might not get their money back right away.

Even though investors know how the market moves, they want to see everything laid out on paper. So, be sure to create a thorough plan before you start doing any work.

The Trouble with Subcontractors...

When you start looking for subcontractors, you might find that doing so isn't easy. You need a really good general contractor that knows the area, has worked on similar projects, and knows the right subcontractors.

The general contractor will then bid out the project and start looking for qualified subcontractors and gauging material cost. But usually, they'll be quite busy with other projects, so this might be a challenge.

This is especially true if you need multiple bids. Some big investors will require multiple bids so that they can compare multiple options. Unfortunately, it could be very tough to get those multiple bids. Some subcontractors will even charge you for a bid because they're so busy.

To avoid this, it's always a good idea to build strong relationships with subcontractors. That way, you'll know who you're working with and what you're looking for. And as you go about completing new projects, you'll know that you have subcontractors to rely on.

Now, building such relationships takes time. You must also be very careful when choosing subcontractors. Let's dive deeper into how to do this right.

Tips for Building Long-Term Relationships with the Right Subcontractors

Every business relies heavily on its people. From this perspective, property development is no exception. If you can't find qualified people for the job, you might encounter many issues along the way.

So, how do you make sure this doesn't happen?

First of all, keep in mind that it's rarely a good idea to hire friends or family members. The only exception is if you're certain that they can do the job right. And especially in these cases when expectations need to be very clear and in writing. Working with someone just because they're close to you can often do much more harm than good.

This is why you should always ensure that a subcontractor has a proven track record. Just because you know them personally doesn't mean you should trust them by default. See if they can produce a competitive bid with a detailed accurate written scope of work.

Second, be sure 100% sure that your subcontractor has proper insurance and licenses. Feel free to ask for their liability insurance, workers' comp, and other relevant insurances and bonding.

Why is this so important?

It's because any issue that a subcontractor causes can create liability for you. They make a mistake, you may suffer the consequences.

For example, we had a client who ran into lots of problems with the IRS because of their subcontractor. The subcontractor was a big company, so the client automatically thought that they were trustworthy.

However, this wasn't the case.

You see, the subcontractor wasn't paying their people correctly. They were paying them on 1099 instead of W-2. At one point, they got audited as the subcontractor couldn't make good on the payroll taxes due to the few workers paid on W2. Remember, many states classify payments to unlicensed subcontractors to be wages, not 1099M payments.

This issue created liability for our client who was the general contractor. They got assigned most of the payroll taxes that the subcontractor hadn't paid.

The client lived with this and their poor choice of a contractor cost them a lot of money.

This brings us to our final tip:

Make sure that your subcontractors pay their people correctly. Ask for the payroll report, and make sure that everything's in order.

If you can't do this on your own, feel free to ask an accountant to go through everything with you. But never assume that everything is right, as you never know what issues you may uncover.

Keep in mind that a lot of contractors cut corners and save as much money as possible. This can reflect poorly on you in all sorts of ways. Set proper expectations for your contractors and subcontractors at the beginning.

When looking for contractors, ask for all the relevant paperwork from them. Go through all the details, and don't start working until you're completely sure they are credible. Find reliable, experienced contractors, and everything will go much smoother.

You Have to Find the Right People

Hopefully, you now understand the importance of having a solid team around you. As mentioned, this is vital to your project's success, so take your time to find the right person for every job.

Remember, spreading yourself too thin is a sure-fire way to leave a lot of room for error. And with investments as large as property development, each of those errors can be very expensive.

Because of this, you need to know your strengths and only focus on what you do best. Don't try being a general contractor before you're confident in your skills and knowledge. Instead, find an experienced contractor that you can rely on to do a good job.

Other than this, outsource everything that you feel like someone else could do better than you. Smart investors know that they don't need to hold the necessary knowledge. Rather, they form a strong network of qualified individuals to do the job.

Once you do this, you can move onto the next stage – finding the perfect land for your development.