



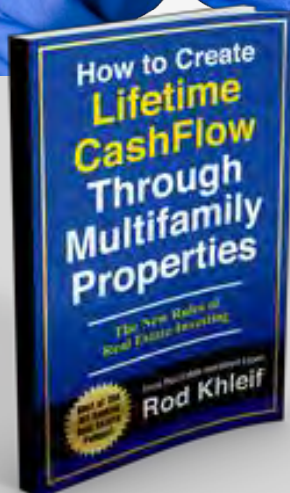
The
Lifetime CashFlow
Academy

Lifetime CashFlow Through Multifamily Properties

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Rod Khleif

Author of How to Create Lifetime CashFlow Through Multifamily Properties

*Host of the #1 ranked Real Estate Podcast on iTunes:
Lifetime CashFlow Through Real Estate Investing*

MODULE

9

LOIs, Contracts & Due Diligence Mastery

Rod Khleif

Lifetime CashFlow

Through Multifamily Properties



The
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LOIs, Contracts & Due Diligence Mastery

Key Points

- The Power of 100% Commitment
- Submitting LOIs & Contracts
- Due Diligence
- Third Party Reports
- The Property Inspection
- Negotiation and Re-negotiation
- Stress Free Property Takeover
- The Power of Becoming an Extraordinary Leader

The Power of 100% Commitment

Find the video in Module 9, Video 1 at 1:48

“Most people fail not because of a lack of desire, but because of a lack of commitment.”

~Vince Lombardi

People who succeed are totally committed. They make a decision to commit and take action. They achieve success because they stick with it.

There's a big difference between having an interest in something and being totally committed to it. When you have an interest, you only work on the goal when it's convenient. But when you're committed, you don't allow any excuses.

Committing to something 100% is actually easier than committing 99%. At 99% you've got wiggle room. Other alternatives can distract you. You have to continually decide whether to quit or not. But when you have decided to commit, there's no possibility of escape. With that decision comes power because you're no longer a dabbler. When you commit 100% you find a bottomless reservoir of strength. Commitment keeps you bonded to your goals.

Momentum and control comes from commitment. Life gets easier when small decisions are eliminated. I decided to write a book two years ago, but when I finally committed to it, I finished it in a very short time.

Total commitment turns into action and that's when the magic happens.

When you have a team and commit to them, they'll commit to you because your unwavering commitment inspires them.

When you're not fully committed, you're always struggling and wasting energy. It's much harder to be only partly committed. Commit 100% and see your world open up.

Life's greatest rewards are reserved for those who demonstrate a never-ending commitment to act until they achieve."

~Tony Robbins

Not everything requires this, but the important things do, like health, relationships, your mission or work.

You'll feel an incredible passion and joy when you're moving toward your goals. But that only happens with 100% commitment.

Commitment requires discipline and determination and life will test your resolve.

When you're completely committed, it sharpens your focus. You're able to recognize opportunities more easily.

Don't get in the habit of breaking commitments, especially to yourself. It conditions you to live an unfulfilled life.

Commit with clarity. Ambiguity makes it easy to break commitments. This is much easier once you find your true purpose.

Practicing a morning ritual helps form the habit of commitment. Starting every day with a routine including things like a big glass of water, light exercise, feeling grateful, writing in a journal, yoga, or reading, gives you something to commit to, which builds your ability to commit to more.

When you encounter challenges along the way, commitment helps you look for a solution, while indecision tends to make you look for an escape.

*Motivation gets you started,
but commitment brings you to your dreams.*

Submitting the LOI & Contracts

Before you submit an offer, you need to know your potential exit strategies from the property.

Do you plan to:

- Refinance?
- Sell?
- Hold it long term?
- How do these strategies meet your investors' return criteria?

Price vs Terms? What's better?

In my opinion, it's always terms. If I can get good seller financing, a low down payment, and monthly payments that make sense for cashflow, I'll pay more if I can get the right terms.

LOI

The Letter of Intent is used to show your intent or desire to purchase a property. It begins the process and negotiation. The LOI starts the conversation with the seller, typically through the seller's broker.

After the LOI is accepted, it's best to meet with the seller directly. The broker can also be there, but it's much more advantageous to speak with the seller than it is to work through the broker only if possible.

The LOI is used prior to submitting a contract to save time and unnecessary legal fees if the deal doesn't come together.

It's a short non-binding document, 2-4 pages long, listing only the main points of your offer. Later, the Purchase and Sales Contract, written by a lawyer, will contain all the legal details and language.

Make sure to see the sample LOI in the document library.

Items in a Typical LOI

- Name of property, if it has one
- Property address
- Property tax identification number
- Legal description of the property, from the county assessor
- Purchase price
- Earnest money deposit amount and due date
- Who will handle escrow
- Payment arrangements such as cash, mortgage, seller financing, etc.
- Projected closing date
- Terms and time frames for your due diligence

Don't commit your earnest money until you've done your due diligence to determine whether this property is worth moving forward on. You want as much time as possible for this. It may be from 30 to 90 days, depending on the market at the time.

- Financing contingency, stating your earnest money is returned if you're not able to get all of your financing.
- Who will create the contract

- Assignment clause
Is the buyer able to assign the agreement to a third party? I typically buy a property under a management LLC and then assign it to a property-specific LLC.
- Broker's commission
- Confidentiality clause
- Non-solicitation clause, committing to work this deal through with you before they entertain other deals
- List of other property sold with the real estate, like lawn care equipment, appliances, vehicles, etc.
- Repair credits
- Seller financing
- Seller paying closing costs
- Who obtains and pays for third party reports

Important Points

You must believe you're offering the best deal possible. Have a confident, but not cocky, attitude. Remember: they are not doing you a favor. You are solving their problem.

It's their loss if they say no. It's their problem. Very often, they will say no at the time, but come back months later when no other deals have worked out.

The Offer or Purchase Contract

Points to Know

- Always use an attorney to write the contract.
- When dealing with partners, always use an escrow agent for all the partnership money. This could be an attorney or title company.
- The contract should always have an effective date in addition to the dates signed by all the parties. All the other deadlines will be based on the effective date.
- We like it when all of the contingencies can only be removed in writing. This gives you an extra layer of protection against missing a deadline and losing your earnest money.
- There's a sample contract in the document library. You'll find many buyer-oriented clauses in it which are meant to give you choices. You won't want to ask your attorney to include all of

them. If it's a fantastic deal, you don't want to push through an onerous contract that would irritate the seller. Be reasonable and get the deal done.

Due Diligence

See the course library for a checklist that you can print out separately with this list of items to research during due diligence.

Don't work from a broker's pro forma when doing due diligence. You want to know what the property has actually done.

You should have already received and studied:

- The last 2-3 years income and expense statements
- The rent roll (Make sure to get the economic vacancy so you know how much rent is actually being paid. Sometimes a rent roll will show the rents being charged, but some of the tenants may not be paying.)

You should have asked and answered all of these questions before the LOI:

- What is the property's age?
- What is the occupancy? Is the property stabilized with at least 80% occupancy? If not, do you see ways to improve it?
- What is the overall condition of the property? Is there any deferred maintenance?
- Do the current rents align with market rents? (You can check with Rentometer.com, Apartments.com, and Craigslist, but remember to compare very similar properties, apples to apples.)
- What is the expense ratio? The average is 50%. Is the expense ratio greater than 45-50% of the gross income? If so, why? Is there a specific reason the expenses are so high? If the expense ratio is very low, this is a red flag too. There could be expenses that were left out of the equation.
- Are there any value-add or reposition opportunities? Are there ways in your control to improve the NOI and raise the value?
- Will the NOI be sufficient to cover the debt service plus still cash flow? Calculate the DSCR.

You should have already asked and answered these questions about the area before you started looking for property there. But now's a good time to review it:

- How's the location/area of the property? You can find out a lot by searching with Google Earth without actually going to the property.
- How does the area look on www.Spotcrime.com?
- What is the condition of nearby similar properties?
- Is the property in an appealing market?
- Is this an emerging market?

Screen Share

- Is population growing?
- Is income growing?
- What's the area's unemployment rate?
- What's the vacancy of similar properties in the area?
- What are others charging for rent?

Measure Demand

As an easy way to measure demand, post an ad on Craigslist for one of the units. If you get no response, then there's no demand. If you get a high volume of calls, it may indicate the rent is too low.

On-Site Inspections

Now that you're under contract, you will need to actually physically visit the property and the area. (You may have done this already, but if the property is not in "your backyard" it's common to have a property under contract that you haven't seen yet.)

Get in the car and drive the neighborhood. Ask yourself the questions that tenants will ask:

- Would I want to live here?
- Are there any jobs around here?
- Would I want to work in this area?
- Is public transportation nearby and accessible?
- Where is the closest grocery store?
- Are schools nearby and what are their rankings? (Check <https://www.usnews.com/education/best-high-schools> to find out.)
- Are there things to do? Can tenants go to the beach, hike, or enjoy other recreational activities nearby? How's the walkability of the neighborhood? (Check www.Walkscore.com) Are there nearby stores, businesses, a movie theater, etc.)
- Would you feel safe living there?
- Would you feel safe collecting rents? Drive past the property at 10pm and on the weekend; do you feel safe? Recheck Spotcrime.com. Remember that one side of a town can be quite a bit different from the other side.) If you're still on the fence about safety, feel free to call the non-emergency number at the local police department. Ask if the property you're interested in has had problems with crime in the past.
- Take a look at the security of the property itself. Will female residents feel safe walking to their apartments from the parking area? Is there a clear line of sight or are there places where criminals could hide? Is the lighting in the parking lot and around units sufficient?

Who's your target renter?

You can find out by looking at who's currently living at the property.

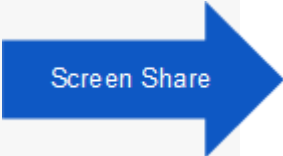
- Percentage of married?
- Ethnic makeup?
- Median age?
- Primarily elderly?
- Students?
- Families?
- Your unit sizes should cater to that marketplace and your optimal tenant for that area. If something is off on this, it may explain low occupancy rates. For example, if most of the units require walking upstairs and the demographic of the area is mostly elderly, that's not something you can fix.
- Basic Demographics
- What's the city's population?
- Population growth?
- Number of households?
- Household growth?

Area Financials

- Median household income?
- Percentage below the poverty line?
- Do an online job search. How many openings do you see? A great online resource for checking job availability is www.indeed.com
- Who are the major employers?
- Is there diversity of employers, not just one big business?

Housing

- What is the percentage of vacant housing? Over 8% can be an issue. Is it trending up or down?
- What is the average home price? We recommend \$80,000 or higher.
- Number of homes vs. apartments?
- What percentage rents?
- Check www.BestPlaces.net for a wealth of this kind of information.



Screen Share

Economic Development

Call, or better yet visit, the Chamber of Commerce and/or Economic Development Office and ask:

- How is business in the area?
- Are there any incentives for investing?
- Have businesses been coming in or leaving?
- Are there any new major employers you know of?

City Planning and Zoning Offices

- Have there been any violations reported on the subject property in the past 5 years? If the city codes department has had to respond to tenant complaints about things like plumbing or pests, these may be problems you'll need to deal with.
- Have any building permits on the property been pulled?

The County Assessor's Office

- What is their opinion on the subject property?
- What is their opinion on the neighborhood?
- Are assessed values increasing? At what percentage?
- How much will the taxes go up based on your new purchase price?
- Have the owners contested the taxes in the past 3 years? If so, what was the outcome? If they haven't, this could be an opportunity for you to reduce expenses.
- What will the taxes increase to based on the new purchase price?

Contractors

Speak to plumbers, electricians, HVAC, maintenance people, etc. who have worked on the property and ask:

- What are the typical or recurring problems?
- What do they think of the infrastructure?
- Do they think anything needs to be repaired or replaced?
- Do they know of any deferred maintenance?

Also, hire new contractors to come out and give you another point of view. The old ones may not be entirely honest about their past work. Have these contractors scheduled for the day of your site visit so you can go through the property with them hour by hour.

Current Tenants

Meet some of the people living in the property and ask:

- Do they like living there?
- Do they plan to stay?
- Is it quiet and safe?
- How are things maintained?
- Do they feel taken care of?
- What changes would you like to see?
- Will they stay or move when lease expires?

Third Party Reports

These are required by institutional lenders.

Phase 1 Environmental

A Phase 1 inspector will come out to check the underlying land and ensure there are no hazardous materials present. They look for things such as underground oil tanks and toxic chemicals.

Engineering Report

Also called the Physical Condition Assessment, this report is done by an engineer who inspects the property and its structure as a whole. They look for anything that will require repairs such as cracks, unsafe balconies, etc.

Property Survey

The survey is required by banks, but make sure to get this when using seller financing too.

It helps to get a copy of the seller's old survey.

This establishes the outline or physical boundaries of the property and determines if a neighbor has built a fence or even another building on the property.

Appraisal

The bank will order this.

Property Inspection

There are several types of inspectors specializing in different areas. Order the ones you think are necessary for the property.

- General Property Inspector
- Engineering inspection
- Termite, wood boring insect, pest inspection: recommended and not expensive.
- On site sewer disposal system inspection
- Lead paint inspection, if the property was built prior to 1978
- Radon gas inspection
- Asbestos inspection
- Urea Formaldehyde Foam Insulation (UFFI) inspection
- Mold inspection, if you see any evidence. This can be very expensive to remedy.

The Inspection Process

Your property inspector should give you a report on the condition of the:

- Roofs
- HVAC, plumbing, electrical
- Foundations

You should also physically walk through and inspect every unit yourself. If you ask to see a few, the seller will only show you the best ones. When walking the units, take pictures or even better have someone walk through with you and take videos. When you watch the videos later, you'll see things you missed.

Financial Inspection

You know it's important to inspect the condition of the physical property, but don't overlook the financial condition.

- Match up bank statements to the rent roll.
- Match up deposits to bank statements.
- Perform a lease audit; check when they expire.
- Ensure that information from the rent roll matches up to the signed leases.
- Log all lease dates and amounts.
- Verify utility bills via bank statements:
 - Water
 - Electric

- Sewer
- Trash
- Read over all contracts:
 - Landscaping
 - Pool service
 - Snow removal
 - Laundry room

When Inspections Reveal Flaws

Don't be afraid to back out of a deal or renegotiate it if your due diligence reveals something seriously wrong. If there were material things left out or misrepresented or if the inspections reveal things are a lot different than you were originally told, then it's okay to re-trade.

Do not abuse this process by going into it with the intent to renegotiate or you'll lose your broker relationship and damage your reputation. Do your homework before making an offer to prevent this.

But do not be afraid to walk away! Don't push through on a deal just because you've spent a lot of time and money on inspections. Sometimes the best deals are the ones we do not buy!

Temper your enthusiasm with the mindset of looking for reasons to back out to protect yourself from mistakes.

Negotiation & Renegotiation Strategies

Negotiation is an indispensable skill when you're working on closing a real estate deal. Like any other skill, it can be learned. Here are some tips:

- Understand that different sellers will have different tempers, education, and experience.
- Always keep negotiations positive.
- Smile and stay calm and relaxed.
- Seek a win-win.
- If things get heated, reschedule for another time.

Preparing for Negotiation

The only way for a win-win to take place is to prepare. So put plenty of energy and thought into this.

Prior to negotiation ask yourself:

- What are your goals for this transaction?

NOTES

- What do you think the other side wants? (That's why it's best to speak directly with the seller instead of going through the broker only.)
- What is most important to them?
- What can you give up in exchange for things you want?
- What do they want that you're okay giving up?
- How important is this deal?
- Will you have an ongoing relationship with this person after the deal is closed? (This would apply to seller financing.)
- What are some of the possible outcomes from this negotiation? Write a list.
- What does each party in the transaction expect?
- What happens if you're unsuccessful?
- What will you do if you don't get what you're asking for?
- What happens to the other side if you're unsuccessful in this negotiation?
- Who loses the most if this negotiation fails?
- Who has the most power in this negotiation?

MODULE 9

Stress Free Takeover of a Property

After closing, there's a lot you can do to ensure that things go smoothly. The current residents may be worried or scared of new ownership. Here are the steps to take:

Notify Everyone of the New Ownership

Tenants

Upon acquisition notify tenants that you are the new owner. Prepare a letter and put one on each door. The letter should include:

- The name, address, and phone number of the property management company
- How the rent can be paid – online, bank draft, or if by check, where to mail or deliver it.

- Where and how to contact the manager for maintenance and other issues.
- Who to contact in case of emergency.

Update Tenant Information

In your introductory letter, include a way for tenants to update their information. You can do this using a paper form, a link on website, or an email address to respond to.

You need them to update or confirm their:

- Name, age, and relationship of all residents of their unit
- Contact information
- Current employer information, including phone number in case of emergency

Utility Companies

They will want to know the new owner's address.

Emergency Services

- Call the local fire and police departments.
- Give them your contact info and your property manager's contact info. If there's a problem they will need to know who to call.

Current Vendors

Update or rewrite any contracts for vendors such as:

- Swimming pool
- Parking lot maintenance
- Landscapers/lawn maintenance
- HVAC
- Plumbers
- Electricians
- Pest control
- Vending machine
- Washer/ dryer equipment owners

Implement a Purchase Order System

- Let your vendors and contractors know that if they do work without a PO, they may not get paid.
- Implement a payment/check cycle on 30-day terms.

Set up Property Specific Checking Account

- Make sure the account is in the name of entity listed on the property title.
- Always keep your personal finances and the property's finances separate, especially if you have partners.

Set Up an Accounting System

Speak with your accountant upon your new acquisition. Here's what you need to talk about:

- Often expenses are misclassified, so be clear on the difference between an expense and capital improvement.
- Decide whether you will use the cash or accrual method of accounting.
- Determine the depreciation schedule and decide on cost segregation.

Create Management Systems

We'll dive deeper into this in the next module, but for now be aware that you and your property manager will need systems in place for the following:

- Rent collections
- Late pay procedure
- Maintenance systems and procedures
- Property upkeep, scheduled maintenance
- Lease-up procedures
- Accounting procedures
- Marketing systems
- Purchase order system

Forms Library

Managing a property is very form and checklist intensive. That's why we've provided sample forms to help you get organized.

The Power of Becoming an Extraordinary Leader

Find the video in Module 9, Video 6 at 9:22

As a business person, you are becoming a leader with all of the responsibilities and rewards that come with leadership.

Leaders think about, look for and talk about solutions.

"If your actions inspire others to dream more, learn more, do more, and become more, you're a leader."

~John Quincy Adams

Followers think about, look for and talk about problems.

Great leaders don't usually set out to be leaders. They focus on their goals and try to make a difference. They do what's right, not what's easy. They have integrity.

The greatest leaders in history were able to translate a vision into reality. They're able to think big.

You're starting a real estate business, so you're taking off your employee hat and putting on your entrepreneur hat. That's a mindset shift. To succeed in this business you'll have to put together a team, and they'll require a leader — you!

"You have to think anyway, so why not think big?"

~Donald Trump

You need to decide to be the leader you'd want to follow.

Great leaders compliment people. They magnify others' strengths, not their weaknesses.

Leaders love what they do so their passion radiates out and inspires others.

"The challenge of leadership is to be strong, but not rude; be kind, but not weak; be bold, but not bully; be thoughtful, but not lazy; be humble, but not timid; be proud, but not arrogant; have humor, but without folly."

~Jim Rohn

They realize God's or the Universe's delays are not denials. They have patience and stay focused on their ultimate vision or goal.

Leaders keep an open mind and remain flexible.

They empower others.

Leaders are personable and friendly. People like to be around them.

Leaders care, and look for the win-win in every situation.

They're decisive. When other people are standing around wondering how to solve a problem, leaders say, "Stand aside. I'll handle it."

Leaders inspire other people to believe in their vision. They're excited and exciting to be around.

Leaders are curious — always learning and growing.

Leaders are always asking the question, “How can I make it better?”

Leaders continually practice and hone communication skills.

They take total responsibility for what happens, and they know that’s not a negative thing. Leaders own it.

Leaders tell the truth no matter how painful it may be.

Leaders love their followers. They instill confidence and bring out the best in other people. To be successful with their team, they know they have to be authentic and transparent in their businesses.

Leaders expect bumps in the road, but stay persistent and focused on their goals.

Leaders hold people accountable, pleasantly but firmly.

Leaders are the creators of their lives. Followers let life happen to them.

“The ultimate measure of a man is not where he stands in moments of comfort and convenience, but where he stands at times of challenge and controversy.”

~Martin Luther King, Jr.

Leadership is fantastic, but it comes with a price:

- It requires focus, hard work, and dedication.
- It regularly brings disappointment.
- It requires sacrifices, but they’re worth it.

Leaders have an incredible opportunity to lift others up, help them grow, and help build their self-confidence. Then they have the joy and satisfaction of seeing their team succeed. Leaders have the privilege of creating magic moments for their team.

Leadership is always about “we” not “me”.

“Leadership and learning are indispensable to each other”

~John F. Kennedy

Leaders bring people together and enroll them in a vision and mission.

Leaders are able to create and leave a legacy for their families and for the good of others.

The real estate business as with almost every business is a team sport. To be a success you need to become a leader.

Our world, our country, desperately needs new leaders – leaders who are not afraid to rock the status quo, and even break a few rules if necessary for the greater good.

Leaders know about giving back. They care about their team, their country, and the world.

Module 9 Most Common Mistakes

- Not fully understanding certain terms/clauses on the LOI and/or contract.
- Working from the broker's and/or seller's pro forma. You only buy on current actuals no matter what.
- Getting an accepted LOI and/or contract and skipping due diligence just to get the deal done. You need to know every reason why you shouldn't do the deal, not why you should.
- Skipping/overlooking things in due diligence. Do not assume anything!
- Not running an ad to test the demand.
- Not walking through each and every unit during inspection.
- Not reading all of the contracts during inspection.
- Mixing personal and business expenses.
- Not following post acquisition steps.