BEST EVER
REAL ESTATE INVESTING ADVICE

PASSIVE INVESTOR Resource

A Guide For Making Informed Decisions when Investing Passively

WITH AN INTRODUCTION TO JOE FAIRLESS, COFOUNDER OF ASHCROFT CAPITAL, AN INVESTMENT FIRM WITH OVER $600M OF ASSETS UNDER MANAGEMENT

> "I AM GRATEFUL TO BE AN INVESTOR WITH JOE. [JOE] HAS A VERY TRUSTWORTHY COMPANY WHO HAS THE UPMOST REGARD FOR THEIR INVESTORS."

- ASH PATEL,
PASSIVE INVESTOR

JOE FAIRLESS Introduction

Since beginning my career in real estate, I have helped people throughout the US make smart decisions with their money through passive investing. Today, I control more than $600,000,000 in real estate assets with my investment firm Ashcroft Capital. I have also written three books on real estate, which have been lauded by experts throughout the industry, and interviewed over 1,700 real estate investors.

In other words, I have the experience, background, success, and motivation needed to guide you in the right direction and maximize your assets. If we work together, *yes*, we will discuss investing a lot when we meet, but you can feel confident that I don't just view this job as numbers and money. **I view it as a way to put good people in the position to do good things.** That is what drives me every day.

OVER $600M

in Real Estate Assets

"WHAT I LIKE BEST ABOUT INVESTING WITH ASHCROFT [CAPITAL] IS THE ACCESSIBILITY AND OPEN COMMUNICATION WITH THE SPONSORS. TACK ON THE ON-TIME DISTRIBUTIONS, THE SOLID RETURNS, AND SIMPLICITY OF IT ALL AND IT JUST MAKES EVERYTHING THAT MUCH SWEETER."

- TAYO OGUNNAIKE,
PASSIVE INVESTOR

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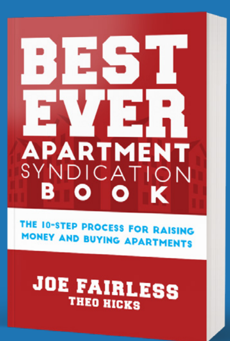

Joe Fairless is the author of the Best Ever Apartment Syndication Book, the ONLY book that provides a proven step-by-step system for completing your first apartment syndication deal.

"I'VE BEEN INVESTING IN REAL ESTATE FOR 15 YEARS AND HAVE HAD A GREAT RUN. I'VE MOVED INTO LARGER APARTMENT DEALS OVER THE YEARS BOTH ACTIVELY AND PASSIVELY. ON THE PASSIVE SIDE I VERY MUCH ENJOY WORKING WITH JOE. JOE HAS A LOT OF INTEGRITY AND I CAN SLEEP AT NIGHT KNOWING HE IS OVERSEEING MY INVESTMENT."

- ALIX KOGAN,
PASSIVE INVESTOR

THE FOLLOWING GUIDE IS FOR ACCREDITED PASSIVE INVESTORS. AN ACCREDITED INVESTOR IS A PERSON THAT CAN INVEST IN SECURITIES BY SATISFYING ONE OF THE REQUIREMENTS REGARDING INCOME OR NET WORTH SET BY THE SEC. FOR MORE INFORMATION, SEE BELOW IN SECTION 2 OF THIS RESOURCE GUIDE.

About The Passive Investor Resource Guide

The sole purpose of this guide is to provide the resources you need to make informed decisions when investing passively in apartment syndication deals.

I first created this guide to fill a need. Before this, there simply wasn't an all-inclusive resource for investors to refer to with the necesary info to help them understand the correct questions to ask, research to do, and things to think about when it comes to passive investing.

I have lead thousands of accredited investors to apartment complex deals and have had thousands of investor conversations based on their experience. The information below was created based on those experiences.

For your convenience, the guide is categorized into three sections:

FIRST, to determine if passively investing in apartment syndications is a strategy that aligns with your investment goals, I have a couple questions to answer.

SECOND, so you can be well versed with what everything means, I have all the apartment syndication terms along with some examples of how the terms are used.

THIRD, to qualify the opportunity so that you protect your hard-earned money, I give you questions to ask to qualify a specific deal, the market in which the deal is located, and the general partner and the team that will implement the business plan.

This guide is just a small sample of the vast ocean of knowledge I have available for FREE on my website. For more information about any of the subjects in this guide, visit BestEverPassiveInvestor.com to learn more.

1.
Knowing Yourself & Your Goals

Active VS
Passive

Before looking at apartment deals or general partners, it's important to know yourself, what type of role you'd like to have in the investment and what your goals are. This starts by determining if you want to be a passive or active apartment investor.

To determine if passive investing is the ideal strategy for you, answer yes or no to the following three questions:

1. Are you busy with your full-time job and other activities but still want to invest in apartments?
2. Do you want to receive the benefits of owning a large apartment building but you don't have the capital and/or expertise to acquire one by yourself?
3. Are you comfortable with someone making business decisions on your behalf?

If you answered "yes" to these three questions, passively investing in apartment syndications aligns with your investment goals.

If you answered "no" to the first two questions, passive investing may still be the route for you, because you require an educational foundation and past real estate or business expertise prior to becoming an active apartment investor. But if you answered "no" to the third question, you shouldn't be a passive investor, because the general partner and their team have 100% control over the business plan.

If you answered "yes" to these three questions but you're goal is to eventually become an active apartment investor, passively investing in a few deals can help you bridge the gap from where you're at to where you want to be from a time commitment, expertise and experience perspective. You will learn the apartment acquisition, management and disposition process in addition to having your involvement in apartment deals on your resume, which will be helpful when speaking to brokers and lenders when you transition to actve investing.

If you have no desire to ever be an active investor and you like your full-time job or want to enjoy your retirement, passive investing is for you.

ACTIVE INVESTING

DEFINITION

The finding, qualifying and closing on an apartment building using one's own capital and overseeing the business plan through its successful execution.

PASSIVE INVESTING

DEFINITION

Placing one's capital into an apartment syndication that is managed in its entirety by a general partner.

What is Your Ideal Passive Investment?

Assuming that passively investing in apartment syndications aligns with your investment goals, the next step is to determine the type of apartment syndication you will invest in.

Distressed Property

A non-stabilized apartment community, which means the economic occupancy rate is below 85% (and likely much lower), due to poor operations, tenant problems, outdated interiors or amenities, mismanagement, deferred maintenance, etc.

Distressed apartment syndications offers little to no ongoing cash flow and a higher potential profit at the end with a higher risk. Therefore, your ideal passive investment are distressed apartment syndications if you want a greater return potential with a greater risk.

Value-Add Property

A stabilized apartment community with an economic occupancy rate above 85% and has an opportunity to be improved by adding value, which means making improvements to the operations and the physical property through exterior and interior renovations in order to increase the income and/or decrease the expenses.

Value-add apartment syndications offers the passive investor a medium to high ongoing cash-on-cash return and medium to high potential profit at the end of the business plan with a lower risk. Therefore, your ideal passive investment are value-add apartment syndications if you want a medium to high return with a lower risk.

2. Important Terminology

General Terminology

The following apartment syndication terms will help you become well versed in passive investing.

ACCREDITED INVESTOR

—

An accredited investor is a person that can invest in securities (i.e. invest in an apartment syndication as a limited partner) by satisfying one of the requirements regarding income or net worth. The current requirements to qualify are an annual income of $200,000 or $300,000 for joint income for the last two years with expectation of earning the same or higher or a net worth exceeding $1 million either individually or jointly with a spouse.

Click here for FAQs about accredited investors answered by the Securities and Exchange Commission (SEC).

NET OPERATING INCOME (NOI)

—

Net operating income (NOI) is all revenue from the property minus operating expenses, excluding capital expenditures and debt service.

For example, a 216-unit apartment community with a total income of $1,879,669 and total operating expenses of $1,137,424 has a NOI of $742,245.

APARTMENT SYNDICATION

—

An apartment syndication is a temporary professional financial services alliance formed for the purpose of handling a large apartment transaction that would be hard or impossible for the entities involved to handle individually, which allows companies to pool their resources and share risks and returns. In regards to apartments, a syndication is typically a partnership between general partners (i.e. the syndicator) and the limited partners (i.e. the investors) to acquire, manage and sell an apartment community while sharing in the profits.

CAP RATE

—

Capitalization rate, typically referred to as cap rate, is the rate of return based on the income that the property is expected to generate. The cap rate is calculated by dividing the property's net operating income (NOI) by the current market value or acquisition cost of a property (cap rate = NOI / Current market value) For example, a 216-unit apartment community with a NOI of $742,245 that was purchased for $12,200,000 has a cap rate of 6.1%.

GENERAL PARTNER

—

The general partner (GP) is an owner of a partnership who has unlimited liability. A general partner is also usually a managing partner and active in the day-to-day operations of the business. In apartment syndications, the GP is also referred to as the sponsor or syndicator. The GP is responsible for managing the entire apartment project.

LIMITED PARTNER

—

The limited partner (LP) is a partner whose liability is limited to the extent of the partner's share of ownership. In apartment syndications, the LP is the passive investor and funds a portion of the equity investment.

SOPHISTICATED INVESTOR

—

A sophisticated investor is a person who is deemed to have sufficient investing experience and knowledge to weigh the risks and merits of an investment opportunity.

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BREAKEVEN OCCUPANCY

—

Breakeven occupancy is the occupancy rate required to cover the all of the expenses of an apartment community. The breakeven occupancy rate is calculated by dividing the sum of the operating expenses and debt service by the gross potential income. For example, a 216-unit apartment community with $1,166,489 in operating expenses, $581,090 in debt service and $2,263,624 in gross potential income has a breakeven occupancy of 77.2%change Commission (SEC).

GROSS RENT MULTIPLIER

—

The gross rent multiplier (GRM) is the number of years the apartment would take to pay for itself based on the gross potential rent (GPR). The GRM is calculated by dividing the purchase price by the annual GPR. For example, a 216-unit apartment community purchased for $12,200,000 with a GPR of $183,072 per month has a GRM of 5.6.

GROSS POTENTIAL INCOME

—

The gross potential income is the hypothetical amount of revenue if the apartment community was 100% leased year-round at market rates plus all other income. For example, a 216-unit apartment community with a GPR of $183,072 and monthly other income of $14,153 from late fees, pet fees and a RUBS program has a gross potential income of $197,225 per month.

INTERNAL RATE OF RETURN (IRR)

—

The internal rate of return (IRR) is the rate, expressed as a percentage, needed to convert the sum of all future uneven cash flow (cash flow, sales proceeds and principal pay down) to equal the equity investment. IRR is one of the main factors the passive investor should focus on when qualifying a deal.

A very simple example is let's say that you invest $50. The investment has cash flow of $5 in year 1, and $20 in year 2. At the end of year 2, the investment is liquidated and the $50 is returned. The total profit is $25 ($5 year 1 + $20 year 2). Simple division would say that the return is 50% ($25/50). But since time value of money (two years in this example) impacts return, the IRR is actually only 23.43%. If we had received the $25 cash flow and $50 investment returned all in year 1, then yes, the IRR would be 50%. But because we had to "spread" the cash flow over two years, the return percentage is negatively impacted.

The timing of when cash flow is received has a significant and direct impact on the calculated return. In other words, the sooner you receive the cash, the higher the IRR will be.

RENT ROLL

—

The rent roll is a document or spreadsheet containing detailed information on each of the units at the apartment community, along with a variety of data tables with summarized income.

UNDERWRITING

—

Underwriting is the process of financially evaluating an apartment community to determine the projected returns and an offer price.

PRO-FORMA

—

A pro-forma is the projected budget of an apartment community with itemized line items for the income and expense for the next 12 months and 5 years, which is an output of the underwriting.

PROFIT AND LOSS STATEMENT

—

The profit and loss statement is a document or spreadsheet containing detailed information about the revenue and expenses of the apartment community over the last 12 months. Also referred to as a trailing 12-month profit and loss statement or a T12.

RENT PREMIUM

—

A rent premium is the increase in rent after performing renovations to the interior or exterior of an apartment community. The rent premium is an assumption made by the general partner during the underwriting process based on the rental rates of similar units in the area or previously renovated units.

For a complete list of terms, visit BestEverPassiveInvestor.com

3.
Questions to Ask the General Partner

Questions

The questions to ask the general partner (GP) fall into four categories:

1. INVESTMENT STRATEGY FAQS:

Questions to ask the GP to gain an understanding of their overall investment strategy and process.

2. SPECIFIC DEAL

Questions to ask the GP about a specific deal they have under contract and are raising money for.

3. MARKET FAQS:

Questions to ask the GP about the market in which they are investing.

4. TEAM FAQS:

Questions to ask the GP to learn the qualifications of them and their team.

BE PROACTIVE

I don't recommend calling up the GP and asking them every question on the list below - otherwise you might drive them clinically insane and that's not good for anyone! Instead, you should be able to pick up most of the info from their website and any info they provide you via written format about their company. In fact, ideally, the general partner will proactively answer these questions when they are presenting a new deal. The purpose of this section is to make you aware of the types of questions to ask and information you need in order to make an educated investment decision.

> "I'VE TRIED OUT MANY DIFFERENT TYPES OF INVESTMENTS. I LIKE INVESTING WITH ASHCROFT FOR A COUPLE REASONS. NUMBER ONE, JOE TALKS TO PEOPLE PERSONALLY, BEFORE YOU INVEST; AND TWO, HE'S GOT SKIN IN THE GAME. HE'S ACTIVELY INVESTING ALONGSIDE OF ME. BOTH OF THE DEALS THAT I'M IN WITH HIM, THEY'VE DONE WELL OR BETTER THAN EXPECTED."
>
> - JEFF ANZALONE, PASSIVE INVESTOR

1. Investment Strategy FAQs

What type of reporting do the investors receive?

Once the deal is closed, the general partner (GP) should send consistent updates on the status of the deal. You may receive updates once a month, which is what my company does. However, some GPs provide quarterly updates. Others provide annual updates. And some don't provide updates at all. The best update frequency will depend on your preference.

In regards to the information included in the update, this varies from GP to GP. Our monthly reports include occupancy rates, updates on the number of renovated units, details on our rental premiums and how they compare to our projections, capital expenditure updates, relevant updates on the market and resident events. Each quarter, we provide a link to the apartment's financial statements, which include the T12 and the rent roll.

Overall, you want to know the status of the business plan and how the rents compare to the projections.

Do you guarantee a return?

General partners should NEVER guarantee a return. If they do, run! Any return offered, like a preferred return, should be a projection, never a promise.

What happens if you can't make the projected cash flow?

Ideally, the general partners projected returns exceed the preferred return offered. That way, if they don't achieve the projected returns, they still distribute the full preferred return. If the actual returns end up being lower than the preferred return, the process is that which was agreed to in the PPM. Generally, the preferred return will accrue until it can be paid with the sales proceeds.

What are the major risk points for this project?

Similar to the question about "what happens if the project fails?", if the general partner (GP) says there are no risks, they are either lying or inexperienced.

The three risk areas associated with apartments are the deal, the market and the team. Therefore, ask the GP about the risks associated with these three areas and what they are doing to mitigate them. You should also determine if they are following the Three Immutable Laws of Real Estate Investing, which are the laws that must be followed in order to mitigate risk, especially in a down economy.

How long do I have to keep my money in the deal?

Before investing in a deal, the general partner (GP) should provide you with the projected timeline, which includes the hold period and the exit strategy of the project. Generally, that is 5 years, and the GP will require you to keep your capital in the deal until the deal sells.

1. Investment Strategy FAQs (cont.)

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Can I pull out my investment?

This varies. But if there is a process for pulling your money out of the deal, it will be outlined in the PPM. The process usually entails you selling your shares to another party with the written consent of the general partner.

How do you make money?

Generally, the general partner (GP) will make money via the acquisition fee, ongoing asset management, equity ownership in the deal and whatever else they decide to charge. All of the fees they charge should be listed in the PPM.

After determining which fees they charge, ask them why. They should only charge fees based on the value they provide to the deal. If they can't explain what value they are providing for each fee, then they shouldn't be charging that fee.

How frequently do I get paid?

The distribution frequency varies and depends on the preference of the general partner and what their team is capable of doing from an administrative standpoint.

The typical frequencies are monthly, quarterly or annually. My company found that the majority of our investors preferred monthly distributions, so that's what we decided to do. So, we aim to distribute the preferred returns on a monthly basis and any profit above and beyond the preferred return is distributed every 12 months. Most likely, you will receive a your monthly, quarterly, or annual distribution 30 to 45 days after the end of the period. For example, if you receive monthly distributions, you would receive the distribution for March at the end of April. Then, you will receive your initial equity investment plus profits from the sales proceeds at the end the sale.

What is the minimum investment?

Most general partners (GP) will have a minimum investment. The more experience they GP has and the larger the project, the higher the minimum.

You want to know what the minimum investment is so that you can determine if you are financially capable of investing in the deal.

The maximum amount of money the GP will likely allow you to invest is typically 19% of the total equity investment. Anything greater than 19% and the passive investor is underwritten by the lender, and they usually don't want that happening. The three risk areas associated with apartments are the deal, the market and the team. Therefore, ask the GP about the risks associated with these three areas and what they are doing to mitigate them. You should also determine if they are following the Three Immutable Laws of Real Estate Investing, which are the laws that must be followed in order to mitigate risk, especially in a down economy.

2. Specific Deal FAQs

Why is the owner selling?

For value-add apartment syndications, the majority of owners are selling because they've reached the end of their business plan. But, some owners may sell because they are distressed in some form or because they originally purchased the property for cash flow and didn't make any value-add improvements.

Is the property being acquired below comparable properties in the area?

The combination of the costs associated with purchasing the property and the capital expenditure costs should be lower than the value of comparable properties in the area. That difference is free equity, which will increase the sales proceeds.

If the acquisition plus capital expenditure costs are equal to or higher than comparable properties in the area, the general partner is paying too much for the property and your profits at sale or equity returned at refinance will be reduced.

What is the going-in cap rate?

The going-in cap rate is based on the purchase price and the current net operating income. You want to know the going-in cap rate so you can compare it to the cap rate in the market. A going-in cap rate that is higher than the market cap rate is a good sign, because that means the property is purchased below market value.

If the general partner's business plan is distressed or value-add, the cap rate isn't as important because the net operating income is lower than what it should be at purchase. If that is the case, you want to know the stabilized cap rate and how it compares to the market cap rate, with the former being higher than the latter as the ideal scenario.

Then, you will receive your initial equity investment plus profits from the sales proceeds at the end the sale.

What's the status of the major systems, like the plumbing, roofs, and HVAC?

Understanding the quality of the major systems is important for the general partner (GP) to determine an exterior capital expenditures budget. Additionally, if the major systems are in bad shape, this is a risk factor and should be addressed with a contingency budget.

Ask them if they or someone on their team inspected these major systems themselves. The only way to know the true state of the major systems is for the GP to see them with their own eyes, as opposed to trusting the owner or the real estate broker broker.

2. Specific Deal FAQs (cont.)

What is the breakdown of the capital expenditures budget?

The general partner (GP) shouldn't just provide you with an overall capital expenditures (CapEx) budget. You want to know how much money is budgeted to each project.

Also, you want to know how they calculated the CapEx budget. More specifically, you want to know if the GP assumed the CapEx costs or if they are based on bids from contractors who inspected the property. The latter is more accurate than the former.

Finally, you want to know what portion of the CapEx goes towards a contingency fund. The contingency should be 10% to 20% of the total CapEx costs.

How do the year 1 income projections compare to the trailing 12-month financials?

If the year 1 income projections are different than the actual trailing 12-month financials (T12), you want to know why. The revenue is based on market rents, loss to lease, vacancy loss, bad debt, concessions, employee and model units and other income. So, if any of these line items differ from the T12, you want to know what the general partner (GP) based those assumptions on and whether or not those assumptions were approved by the property management company.

If the GP is a value-add investor, then the T12 will always differ from the year 1 projections because the market rents are being increased.

What annual income growth factor is being used?

A conservative annual gross potential income growth factor is between 2% to 3% after stabilization. This factor is the projected natural growth in revenue.

Some general partners (GP) will base this factor on historical rent growth, which may be lower or higher than 2% to 3%. Rent growth factors 4% or higher are aggressive and if you run into such a case, the GP should have ample evidence to prove why they've assumed a higher number.

What assumptions are being used to

You want to know if the annual tax assumption is based on what the current owner is paying or if it is based on the purchase price. The latter is the correct approach.

The tax assumption can be calculated by finding the tax rate on the county's auditor site and multiplying it by the projected purchase price.
Ask them if they or someone on their team inspected these major systems themselves. The only way to know the true state of the major systems is for the GP to see them with their own eyes, as opposed to trusting the owner or the real estate broker broker.

3. Market FAQs

How do you qualify a market?

You want to know what market factors the general partner looks at when qualifying a market. Important factors include unemployment change, population growth, population age, job diversity, the top employers and supply and demand.

How is the school district?

One of the factors a prospective tenant will take into account when moving to an area is the quality of the school district. Even if the target tenant demographic are not small families, a quick way to gauge the overall quality of a market is the school district. Look at the elementary, middle and high schools and see how they rank.

A website to find information on the quality of the local school district is GreatSchools.org.

Are there any crime issues?

No one wants to live in a high crime area. Look at the crime stats for the market. If there is a specific deal, look at the crime stats of the neighborhood.

More specifically, look at the crime trend. Even if it is relatively high, a downward trend is a good sign. A good resource for crime statistics is CrimeReports.com.

What is the median income?

You want to know the median income of the area in order to determine if the demographics income levels support the rent projections. Generally, people spend 25% to 35% of their annual income on home expenses. Therefore, confirm that the median income is at least 3-4 times higher than the annual projected rent.

The United States Census Bureau keeps details data on median incomes across the country.

What is the market vacancy rate?

The market vacancy rate is essentially the average multifamily vacancy rate in the market. However, a more accurate market vacancy rate is based on a handful of recent sales.

Ask them what the market vacancy rate is and how it was calculated, and then compare that rate to the assumed vacancy rate for the specific deal.

3. Team FAQs

What percentage of your investors have invested multiple times?

You want to know what percentage of the passive investors are returning investors and what percentage are first-timers.

Because return investors have already passively invested in at least one deal, having a large percentage of return investors signals that you are dealing with a high-quality general partner (GP). However, if the GP has only completed a handful of deals, they may not have many return investors because the return investors haven't received their initial capital back yet.

What is your experience?

Determine how many deals they have completed and how those deals actually performed when compared to the projected returns. If the general partner (GP) has had past deals that underperformed when compared to the projections, it isn't necessarily a deal breaker. A good follow up question would be "what processes have you put in place to reduce the likelihood of an underperforming deal?"

I would also take into consideration if a GP hasn't successfully taken a deal full cycle. While this can be offset by an experienced team, there is still more risk when going with a GP without a proven track record.

Do you currently have any deals under contract?

This is a question you would want to ask during your first conversation with a general partner. If they have a deal under contract, ask them some of the questions I outlined in the "Specific Deal FAQ" section. You will have a better understanding of their business plan when they explain it for an actual deal than for a hypothetical deal. Also, if they currently have a deal under contract, ask them how much capital they have left to raise. Maybe, this can be your first passive investment.

What are my responsibilities?

As the limited partner, your sole duty involves the funding of the deal. After that, the process should be hands off except when reviewing the investor reports and doing your taxes at the end of the year

What are your responsibilies?

Generally, the general partner will find the deal, review and qualify the deal via underwriting, make and negotiate the offer, coordinate with professional property inspectors, find the best financing options, coordinate with attorneys to create the LLC and partnership agreements, travel to the property to perform due diligence and market research, hire and oversee the property management company and perform ongoing asset management, which includes lender conversations, overseeing the business plan and ongoing communication.

For the complete Guide or to reach out to me to learn more, visit

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