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Guide For Real Estate Investors On-the-Go

Are You a Commercial Real Estate Investor?

The first step before investing in commercial real estate is to consider the type of person you are, your situation, and what you're looking for.

1. Ask yourself these questions to determine if you have what it takes to be a commercial investor:

- What kind of property are you looking for?
- Are you looking to use the building for your own business, rent it, build equity, and/or something else entirely?
- Where do you want to invest (location)?
- What's your situation regarding cash, financing, and/or ability to make a down payment?
- Would you be willing to partner with someone else?
- What's your risk tolerance?
- How much time can you commit to the property?
- How much work are you willing to put into the property?
- What skills/knowledge are you bringing to the table?
- What kind of property manager will you need (or not)?
- Are you willing to do the duties of being a landlord?
- Are you ready/willing to make an investment/purchase of this size?

2. Learn commercial real estate vocabulary (and accept the learning curve)

There's a lot of vocabulary and acronyms in commercial real estate that you're likely unfamiliar with. It's helpful to be savvy on some of the terms. This will make this process and working with people in the industry easier.

Here are some common terms to get started with:

- Loan-To-Value (LTV): A ratio of how much money you're asking from a lender vs. the total value of the property.
- Debt Service Coverage Ratio (DSCR): Net operating income over total debt service.
- Capitalization Rate (Cap Rate): Income of the property divided by the total value of the property.
- Cash on Cash: Annual income over how much you actually invested. The amount invested could be just the amount your down payment was.
- Vacancy Rate: Percentage of properties that are vacant in a time period in a given area.
- Usable vs. Rentable Square Feet: **Checkout the difference between these.**
- Ad Valorem: A tax based on the assessed value of a piece of property.

These are just some of the terms. **Loopnet.com has a great glossary of commercial real estate terms.**

3. Visit and consider many properties. Do your homework on each.

Consider and tour many different properties. Figure out what works and doesn't for each of them. Consider the most important things for each one including price, location, condition, and allowed use.

The importance of location can't be overemphasized. Properties located near universities, hospitals, or downtown areas will generally have a higher value and sell more quickly.

Above all, you're searching for a "fit" with your property in terms of price, location, use, and investment required.

Key calculation for any property is for it to be in the black after subtracting PITI (principal, interest, tax, and insurance) from the annual revenue earned from rent.

Here are a few more questions to consider for each property you're interested in:

- What is the property currently used for?
- What can/can't it be used for?
- How much rent/income does the property currently generate annually?
- How much are taxes?
- What needs to be replaced or repaired soon?
- Why is the owner selling?
- How is the area around the property? Any major upcoming changes?

Also see this **more extensive checklist** of questions to ask about properties.

4. Find the experts you'll need

Buying commercial real estate is often a complex process. You'll likely need to hire experts to help with some of the steps. Which and how many experts depends largely on the type of property you're purchasing.

At the very least, you'll an accountant, commercial real estate lawyer, commercial realtor, and a mortgage broker.

If the property is more complicated, you could need other specialists like tax experts, or environmental specialists, just to name a few.

5. Figure out your financing

Most investors will need commercial financing in order to purchase the property.

Find out what your options are as for as: LTV, down payment required, interest rates, minimum DCSR, credit history and score and lending locations (city vs. rural). Also, you need to know types of properties lenders will finance. Be very clear on how much money you need to bring to the table.

If traditional financing methods will not work for your situation, try a more creative method for financing/purchasing the property. Would the owner be willing to help with financing? This is known as seller financing or seller carry back. Or, perhaps a joint-venture arrangement may work.

6. Make an offer (with your lawyer's approval!)

Don't sign anything without your lawyer's review first.

You'll need to execute a letter of intent (LOI) if your lawyer gives you the ok to sign the contract. The LOI outlines the basic terms of the transaction. Make sure your lawyer explains all details of the written agreements so you know exactly what your rights and obligations are. Also, your lawyer should make sure the LOI is not binding in case something goes wrong with the property, financing or anything else that could go wrong.

7. Due Diligence and Escrow

This is where it gets more real because money is about to change hands. You'll need to dot all the i's and cross all the t's.

You'll need to get an ALTA (American Land Title Association) survey ordered. This provides valuable information such as boundary lines, location of the main building (if there is one) including improvements, location of secondary buildings, the identification of easements (which are access rights by different service companies such as water, gas, telephone, railways and other utilities).

You and the seller will need to find an escrow officer who will be the neutral 3rd party overseeing the transaction. They will help with the transfer of deeds and funds. They make sure both parties are protected in the transaction.

The final closing escrow documents will include things like a quitclaim deed, non-foreign affidavit, title affidavit, bill of sale, sale and assignment of contracts, warranties and supplier guarantees.

Finally, you (the buyer) are given a due diligence time period with which to make sure all the documentation about the property is correct. This is where you triple check everything the seller told you about the property.

If something strange or wrong comes up in your inspection of the property, you have the right to tell escrow to cancel the transfer of funds.

Property Metrics **has an excellent checklist** for the final processes involved in purchasing commercial real estate.

Buying commercial real estate can be a lengthy process but if you follow these steps, it should make the process go smoother.

Source: 42 Floor