JUMPSTART TRAINING WORKBOOK

Notes

Welcome from Ken Weinstein, founder of Jumpstart

I'm excited you decided to enter the world of residential real estate and community development. Jumpstart has grown from a couple of students sitting in my office in 2015 to four classes a year of 65 mentees at a time—and that's just in the Germantown section of Philadelphia. Now, as we're expanding to other neighborhoods, cities, and towns, it's an honor to share my experiences and ideas on developing real estate thoughtfully and strategically, so that the neighborhood wins as much as you do.

I'm grateful to the Philadelphia office of the Local Initiatives Support Corporation (LISC) and The Barra Foundation, which have made the expansion and improvement of Jumpstart possible. You should use this workbook to dive into the world of residential real estate development but, in the end, there is no shortcut to learning by doing. After completing these Jumpstart sessions, I hope you'll aggressively continue on this exciting path that can change more than a house or a neighborhood. It can change your life.

LISC Philadelphia

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SESSION 1

In Session 1, you'll...

1. develop ***skills***
    - assess risks/rewards
    - evaluate your own strengths/weaknesses

2. gain ***knowledge***
    - identify criteria for choosing a neighborhood
    - learn how to find properties

3. obtain ***tools***
    - explore websites and Facebook groups about local real estate happenings
    - find sources for researching properties and their owners
    - locate a list of networking organizations to join

An Overview of Jumpstart

History and Success of Jumpstart Germantown

Ken Weinstein, founder of Jumpstart Germantown and Jumpstart Philly, is the President of Philly Office Retail, a commercial and mixed-use real estate development company based in Philadelphia. He has three decades of entrepreneurial, political, and real estate experience:

- Formerly owned a series of eateries: Trolley Car Diner, Trolley Car Café, Trolley Car Station, and Cresheim Cottage Café, all in Philadelphia.
- Chairs the Philadelphia Housing Development Corporation (PHDC), a quasi-governmental agency that helps low-income people continue to live in their homes by providing basic systems home repairs.
- Founded the Mt. Airy Business Improvement District (BID), Trolley Car Teachers' Fund, Trolley Car Table Tennis Club, and Wage Change.
- Served as a Director/Organizer of Valley Green Bank, a community bank that helped revitalize neighborhoods by providing commercial real estate loans.
- Mentored NFL players in real estate development at the University of Pennsylvania's Wharton School.

What made Jumpstart Germantown and Jumpstart Philly a success?

Social entrepreneurs, like Ken Weinstein, believe in starting new, innovative projects to solve problems and create opportunities. Seeking win-win opportunities enhances your bottom line. His philosophy: Follow your passion and continue to learn every day.

The Jumpstart Mentoring Program is growing.

- Ken conducted the first Jumpstart Germantown mentoring session in April 2015.
- Since then he has graduated more than 1,000 people from his Jumpstart Germantown Mentoring Program and hundreds more through Jumpstart Philly.
- There's been an overwhelming interest in learning responsible residential real estate development and many participants have made major investments in their community.

Jumpstart is spreading.

- Jumpstart initiatives have already spread to Philadelphia's Kensington, Tioga, Hunting Park, North Philly West, West, and Southwest neighborhoods, with new start-ups planned in the years ahead. With the recent addition of Jumpstart programs in Wilmington, DE, and Norristown, PA, the potential for neighborhood revitalization is endless.

The 3 Jumpstart Initiatives

1 Mentoring Sessions

- 9 hours, or more, of instruction
- on-site visit to a residential construction project
- at the conclusion of the sessions, each mentee is assigned a mentor to help with their development projects (evaluate pro formas, assess due diligence, walk through properties, etc.)

2 Developers' Network

- meets 4 times a year
- panel discussions, guest speakers, and opportunities to connect with more experienced developers and community stakeholders

3 Loan Program

- offers high LTC (Loan to Cost) loans and quick approvals
- acquisition and construction lending
- reasonable, fixed interest rate and fees
- loan process that resembles a bank loan

TOOL 1.1

YOUR JUMPSTART "TO DO" LIST

- [ ] Attend sessions & connect with a mentor
- [ ] Apply for the Developers' Network & "like" the local Jumpstart Facebook group
- [ ] Determine your investment goals and strategy
- [ ] Identify your team (bankers, investors, advisors, realtors, contractors, lawyer, accountant, designer, etc.)
- [ ] Find a property and put it under agreement of sale
- [ ] Conduct your due diligence
- [ ] Obtain short-term acquisition and construction financing, through Jumpstart or elsewhere
- [ ] Renovate the property
- [ ] Lease, sell, or live in the property
- [ ] If holding the property, obtain long-term financing

Jumpstart Philosophy
Doing Well by Doing Good

A. Improve your community

By focusing on ***social impact real estate development***, Jumpstart helps developers:

- remove neighborhood blight
- target scattered sites, not “urban renewal”
- create a healthy mix of affordable housing and market-rate housing
- increase property values
- avoid gentrification through slow, steady growth

B. “Grow the Pie”: Share Resources

The Jumpstart approach is more collaborative than competitive. By sharing resources and information, Jumpstart participants can do more together than they can do alone.

Instead of fighting over a piece of the pie, focus on growing the pie!

- Form networks and partnerships with other realtors, developers, and owners, and share information instead of hoarding resources.
- In real estate, there’s an “80/20 rule.” Only 20 percent of people in real estate openly share information and resources. Be a part of the “20 percent.”

The Jumpstart Facebook page and Jumpstart Developers’ Network are two ways to share information and resources.

Jumpstart Philosophy *(continued)*

Doing Well by Doing Good

C. Be a good neighbor: Gain community support and a marketing advantage

- Take the time to connect with neighbors near your development project and build their trust.
  - Knock on doors and introduce yourself.
  - Leave a note, with contact information, if nobody is home.
  - Use neighbors as a marketing tool and eyes and ears on your project.
- Be a neighborhood partner, not an adversary.
  - Explain how your development project benefits the community.
  - Don't minimize, ignore, or belittle neighborhood concerns or suggestions.
- Attend neighborhood meetings and get to know the larger community.

D. Invest in your future: Create a nest egg

Create a financial nest egg, so you and your family can live more comfortably, by investing in your neighborhood.

E. Change the face of development: Encourage diversity

One of the goals of Jumpstart is to support women and people of color who want to enter the field of real estate development.

What You Need to Jumpstart and Succeed

1. Be a sponge—never stop learning and continue to improve

2. Be willing to take risks—development isn't for everyone

3. Embody these qualities
    - authentic and trustworthy
    - responsive
    - knowledgeable
    - organized
    - patient
    - persistent
    - aggressive
    - have "fire in the belly"
    - use common sense and "street smarts"
    - be action-oriented
    - attend to the nitty-gritty

"Young, scrappy, and hungry"

—from the Broadway show *Hamilton*

4. Get going. It's on you to get it done!
    - network with other developers and real estate groups
    - use your mentor
    - engage potential partners and team members
    - start looking for properties
    - ask for help

TIP: Get your real estate license but don't become an agent—just use the information from the class to learn the ins and outs of real estate.

ACTIVITY

IDENTIFY YOUR STRENGTHS AND WEAKNESSES

1. Grab a partner.

2. Find out which of these qualities are among their strengths:
   - authentic and trustworthy
   - responsive
   - knowledgeable
   - organized
   - patient
   - persistent
   - aggressive
   - have "fire in the belly"
   - use common sense and "street smarts"
   - are action-oriented
   - attend to the nitty-gritty

3. Find out how they developed these qualities.

4. Have your partner ask you questions about your strengths.

5. Compare notes on weaknesses.

6. Tell the group about your partner's strengths and weaknesses.

The 7 "JumpSteps" of Residential Real Estate Development

SESSION 1

JumpStep 1: Create a ***Development Strategy*** & Identify Your Team

JumpStep 2: ***Source a Property***

SESSION 2

JumpStep 3: Do Your ***Due Diligence***

JumpStep 4: Find Your ***Financing***

JumpStep 5: Develop ***Design*** & Procure Permits

SESSION 3

JumpStep 6: Customize ***Construction***

JumpStep 7: ***Lease/Manage/Sell*** Your Property

TOOL 1.2

GLOSSARY OF REAL ESTATE DEVELOPMENT TERMS

Put a checkmark (✔) in the margin next to each term you're familiar with. Put an asterisk (✱) next to those you're unfamiliar with. Review this list again after each session and update your checkmarks.

A

ABATEMENT: A reduction in the level of taxation an individual or company faces. A common type of abatement is property tax abatement, where property owners are exempt from Real Estate Taxes on improvements to existing properties or new construction for a set amount of time.

ABSTRACT OF TITLE: A historical summary of the recorded instruments and proceedings on the title of a property. Also known as Title Abstract.

ACCRUED INTEREST: The interest on a loan that has accumulated since the principal investment, or since the previous coupon payment if there has been one already.

AMORTIZATION: Paying off debt with a fixed payment schedule, in regular installments over a period of time, that consists of both principal and interest.

APPRECIATION: The increase in the value of a property due to changes in market conditions, inflation, or other factors. Investing based on appreciation assumes returns will come later, once the property appreciates significantly and you can collect on that increase. Appreciation is not guaranteed and is based on speculation.

ASSESSMENT: The local government's required effort to determine a basis of property value for real estate tax purposes. It is performed by an assessor, who may use public records (which can be outdated) rather than visit the property personally. The assessment value is NOT a reliable indicator of sales price or fair market value.

APPRAISAL: An evaluation of value to determine the current market value (sales price) of a specific property at a specific time. An appraiser (who does the appraisal) must be licensed, approved by the bank, and provide a valuation that represents the "fair" sales price of the home.

B

BALLOON LOAN: A type of loan that does not fully amortize over its term, requiring an oversized payment ("balloon payment") at maturity to repay the remaining principal balance of the loan.

BUILDERS RISK INSURANCE: A type of insurance that protects a person's or organization's insurable interest in materials, fixtures, and/or equipment to be installed during the construction or renovation of a building or structure, should those items sustain physical loss or damage from a covered cause.

C

CAPITALIZATION (CAP) RATE: The ratio of Net Operating Income (NOI) to property asset value. An estimated percentage return, it can be used to compare potential deals. Calculated by dividing Net Operating Income by Current Market Value. (For example, for a property listed for sale for $100,000 that generated a NOI of $10,000, the cap rate would be $10,000/$100,000 [or 10%].)

CASH-FLOW: The profits you collect each month from a rental property. You collect the rent from the tenant (a.k.a., gross income) and subtract your expenses (mortgage, taxes, insurance, repairs, management fees, vacancies, etc.) and that leaves you with your cash flow (a.k.a., net income).

CASH-OUT REFINANCE: The instance when a borrower refinances their mortgage at a higher amount than the current loan balance, with the intention of pulling out money.

CLEAR TITLE: A title that is free of liens or legal questions as to ownership of the property.

COLLATERAL: A property or other assets that a borrower offers a lender to secure a loan. If the borrower stops making loan payments, the lender can seize the collateral.

COMPS: "Comparable sales": the recent sales of similar properties in nearby areas, used to help determine the market value of a property.

CONTINGENCY: Money put aside for unforeseen expenses that are possible but cannot be predicted with certainty. (We suggest using a contingency of 15% of construction costs for rehabs. Contingency for new construction is usually lower.)

D

DEBT SERVICE: The cash required for a particular time period to cover the repayment of interest and principal on a debt.

DEED: The legal documents that transfer ownership of real property from the old owner to the new. Many types of deeds provide various level of protection to the buyer; the general warranty deed provides the most protection, and the quitclaim deed provides the least.

DUE DILIGENCE: The investigation and review of a property to determine any problems, liabilities, or other issues that a buyer should consider prior to purchasing a property.

E

EARNEST MONEY DEPOSIT: The deposit a buyer makes at the time of submitting an offer to demonstrate the true intent to purchase. Also called a "binder" or "good faith deposit."

ENCUMBRANCE: A claim, lien, charge, or liability attached to and binding upon real property.

ESCROW: An item of value, money, or documents that transacting parties give to a third party, to be delivered upon the fulfillment of a condition.

ESCROW ACCOUNT: An account in which funds are set aside for specific payment(s).

F

FLOATING RATE: Another name for an Adjustable-Rate Mortgage; a type of loan where the interest rate is not fixed but allowed to "float" or vary over time.

FORECLOSURE: When a homeowner is unable to make full loan payments on their mortgage, allowing the lender to seize the property, evict the homeowner, and sell the property.

G

GRANTEE: The person receiving property ownership, commonly known as "the buyer."

GRANTOR: The person or legal entity transferring property ownership to another. The grantor is usually the current property owner.

GROSS LEASE: A lease in which the landlord pays all expenses associated with owning and operating the property.

H

HOLDING COSTS: Costs associated with owning a property during construction. This may include property taxes, interest, insurance and utilities, and/or vacancy.

I

INTEREST-ONLY LOAN: A method of loan amortization in which the borrower pays interest periodically over the term of the loan and pays the entire original loan amount at maturity. (Jumpstart Germantown Loans are interest-only loans.)

L

LIEN: A legal claim against a property that must be paid off when the property is sold. A mortgage or first trust deed is considered a lien.

TOOL 1.2 (CONTINUED)

GLOSSARY OF REAL ESTATE DEVELOPMENT TERMS

M

MATURITY: The date on which the principal balance of a loan, bond, or other financial instrument becomes due and payable.

N

NO CASH-OUT REFINANCE: A refinance that is not intended to put cash in the hands of the borrower. Instead, the new balance is calculated to cover the balance due on the current loan and any costs associated with obtaining the new mortgage. This is also known as a "rate and term refinance."

O

OPEN-ENDED MORTGAGE: A mortgage that may be refinanced without rewriting the mortgage contract.

ORIGINATION FEE: An up-front fee a lender charges for processing a new loan application, used as compensation for putting the loan in place. Also called financing fee or commitment fee.

P

PRE-APPROVAL: A write-up of a loan to show proof of funds without any legal signatures binding the borrower to the loan. It means that a borrower has completed a loan application and the loan provider has preliminarily approved the borrower for a loan.

PRINCIPAL: In a loan, the amount borrowed or the amount still owed on a loan, separate from interest.

PRO-FORMA: A set of calculations that projects the financial return a proposed real estate development is likely to create.

PROMISSORY NOTE: A signed document containing a written promise to pay a stated sum of money to a specified person at a specified date.

PURCHASE OPTION: A lease agreement under which the user/tenant has the option to purchase the leased asset/property at a specified price at the end of the lease term.

R

RIGHT OF FIRST REFUSAL: A provision in an agreement that requires the owner of a property to give another party the first opportunity to purchase/lease the property before they sell or lease it to others.

S

SECURED LOAN: A loan that is backed by collateral (a.k.a., a security).

SHORT SALE: A sale of real estate in which the net proceeds from selling the property will fall short of the debts secured by liens against the property.

T

TITLE INSURANCE: Insurance that protects the lender (lender's policy) or the buyer (owner's policy) against loss arising from disputes over ownership of a property or liens against a property.

U

UNDERWRITING: The determination of the risk a lender would take on if the lender were to approve a particular mortgage loan application.

V

VACANCY COST: The cost to an owner of not having a tenant in a rental property. Calculated by multiplying total annual rent by the vacancy rate.

VARIANCE: A specific waiver to allow deviation from current zoning requirements of a property. If granted, it permits the owner to use the land in a manner not normally permitted by zoning law. It does not, however, change the zoning law. A city or town's Zoning Board is generally the grantor of a variance.

JumpStep 1
Create a Development Strategy & Identify Your Team

1.1 Why invest in a neighborhood?

- ***Market history***: Assessing housing values and rents over time and recent trends in the neighborhood (via reports, real estate agents, developers, residents)
- ***Affordability***: Opportunity to buy with less money down (lower risk)
- ***Price stability***: Slow, steady growth over time = more recession-proof (lower risk)
- ***Interest***: Pursuit of more attractive housing stock (But don't "fall in love" with your real estate.)

1.2 Assess risks and rewards: Be aware of your expectations

High risk = Higher expected return; Low risk = Lower expected return.

<u>Risk factors</u>

- ***Time & Money***: A project with a limited scope (e.g., cosmetic changes only) lowers your risk. A gut rehab increases your risk.
- ***Neighborhood volatility***: Stable rents or sale prices lower your risk.

<u>Potential rewards</u>

- ***Profit***: Take into account the property's expected appreciation and your annual ROI. (See the Acronym worksheet on page 23.)
- ***Social impact***: How will your investment improve the neighborhood?

1.3 Determine the ***best strategy*** for you

A. Development ***options***

Where?

- urban vs. suburban
- infill vs. sprawl

Note: Jumpstart focuses on residential, scattered-site rehab (as opposed to commercial rehab or sprawling suburban development).

What?

- market-rate housing vs. low/moderate-income housing vs. workforce housing
- new construction vs. rehab

JumpStep 1 *(continued)*

Create a Development Strategy & Identify Your Team

How?

- appreciation vs. cash flow
- buy, rehab, and sell (flip)
- buy, rehab, and hold (rental)
- buy, rehab, and live in (home ownership)

B. Find your ***niche***

Focus on a type of real estate you understand. Do you have a feel for:

- commercial, residential, or mixed use?
- low-income or high-end?
- a specific rental market (e.g., single-family or multi-family)?

C. Enter into ***partnerships***: Expand your capacity!

- Choose your partner(s) wisely. Find people whose strengths (and weaknesses) complement yours.
- Talk about expectations up front.
- Put everything in writing.
- Have similar goals and a mutually agreed-upon exit strategy.
- Have respect for each other.

D. Devise a ***"game plan"*** for the property

What will you do with the property?

- single family or multi-unit?
- gut rehab or heavy cosmetic work?
- use existing layout, or demo and reconfigure?
- sell, rent, or live in?

Devise a series of options/strategies:

- rehab individual units as tenants leave—better cash flow
- rehab all units at once—lower construction costs
- rehab building when neighborhood conditions demand higher-quality units and increased rents

1.4 Avoid *mission creep*

Stay on course. Don't make abrupt changes in strategy.

- If your niche is buying and renovating single-family row houses, don't suddenly buy multi-family housing. Do what you do best, and don't get distracted.
- Don't open a retail or restaurant business—unless that's your goal! This will only slow you down and could negate your cash flow. Make deliberate choices and don't fall into a sudden change of direction. Stay focused!

1.3 Do your *legal legwork*

Individual ownership vs. corporate ownership

- A limited liability company (LLC) creates a corporate veil that can protect the owner personally from liability
- Buy with an LLC, if that's the end game—it's costly to transfer a title later from an individual to an LLC
- Evaluate the risks of purchasing multiple properties in one LLC vs. the cost of creating and maintaining multiple entities
- What's involved in creating an LLC?
    - filing paperwork
    - time (1–2 weeks to file)
    - operating agreement

JumpStep 2
Source a Property

Finding an investment property is the most difficult part of the real estate development process!

2.1 ***Where*** to find properties

- sheriff sales (mortgage or tax sales) (see **TOOL 2.1** on the next page)
- public auctions
- conservatorship process
- "for sale by owner" (FSBO) properties
- properties with liens (buy liens and foreclose)
- government or land bank owned
- short sales
- bank sales/foreclosures (real estate owned [REO])
- MLS hot sheets—what's already "on market"
- wholesalers
- HUD/VA owned
- other?

2.2 ***How*** to find properties (strategies/people/places)

- build relationships with local real estate brokers/agents
- go door to door
- network/word of mouth/social media—"off market"
- marketing: flyers, posters, letters to current property owners
- government agency websites

There are many ways to find available properties. Pick a couple, and get aggressive! They're there if you're ready, willing, and able.

TOOL 2.1

WHAT TO LOOK FOR AT A SHERIFF SALE

Adapted from a Brixsy *article (by Chris C, September 27, 2015)*
http://blog.brixsy.com/3-things-to-look-out-for-at-the-philadelphia-sheriff-sale

Survey the scene

Who's there:

- investors (and wanna-be investors) looking for their next deal
- attorneys representing lenders
- homeowners who may be faced with losing their home

Look for the "insiders"

In a room of hundreds of people, you'll notice some "pros" who clearly know each other—because they're there every week. Look how they nod to each other and exchange knowing glances.

Review the list of properties in advance

The Sheriff's Office website will post in advance the list of properties to be sold. Research and drive by the properties that interest you. Figure out what each property is worth and narrow down your list to the ones you like the most. Try to get inside the property, if possible.

Buyer beware

"It's a calculated risk. Just do your homework."

Many real estate investors don't dare go the sheriff sale route at all because they've been burned in the past. *Even the pros who regularly buy properties at the sheriff sale get burned.*

What can cause problems? Debt, judgments, and liens that hang on a property after auction and the risk of right of redemption. The sheriff's office warrants that all property is sold "free and clear of liens and encumbrances." The practical reality of this is not so clear.

3 common things that almost always happen at a sheriff sale

1. ***A guarantee is only as good as the people behind it.***
   Property goes up for sale at auction and has a list of judgments and liens other than the taxes or mortgage it's being sold for. Solution: Target those properties that are relatively free of liens. This will "save you tons of time, reduce your risk, and at some point probably save you real money. It's also a strategy that may have you bidding with less competition."
2. ***Check the distribution list.***
   "For mortgage foreclosure sales, get the distribution list…from the law firm that represents the foreclosing lender. (You'll probably have to call them before the sale, and most will put you on a regular email list.) This lists all of the liens and judgments that are planning to be paid off with the money from the sale. You can also get the list of all creditors and lien holders that have been notified of the sale.

TOOL 2.1 (CONTINUED)

WHAT TO LOOK FOR AT A SHERIFF SALE

Adapted from a Brixsy *article (by Chris C, September 27, 2015)*
http://blog.brixsy.com/3-things-to-look-out-for-at-the-philadelphia-sheriff-sale

"...Do a search of title and compare this list to judgments and liens that are of record. [Any] not planning to be paid off...may end up being your problem if you buy. If a creditor wasn't notified properly, their lien may not just disappear with the sale and you as the owner may have a big problem."

3. Beware the right of redemption

A property ends up at a Sheriff Sale because of either:

- Delinquent taxes OR
- Mortgage foreclosure

Tax sales are much trickier because of:

- Proof of service
- Right of redemption

"Fortunes have been made and lost at...tax and mortgage foreclosure sales... if you're not prepared, you're sure to lose."

"**Proof of service** means that the owner of the property was properly notified that they were about to lose their property. Law firms do a good job of this for mortgage foreclosures but the city doesn't when it comes to tax sales. It's expensive to hand deliver notice, so they typically just send letters. The problem is, there's no real proof that the letters were ever received and the homeowner was properly notified. The law is very much on the side of the homeowners here, and there have been many cases when homeowners made successful arguments that they didn't know about the sale.

"Hence the **right of redemption**. [In Philadelphia] This means that homeowners that lose their home for tax delinquency have 9 months after the sale to come up with all of the money (including any penalties, interest and attorney's fees) and they get their house back. Even if you've bought it fair and square, you have no rights here. You have to give it up. You'll get what you paid back plus 10%, but any other improvements and money in is lost. That's why no title insurance company will insure a tax sale property until at least a year after the sale."

How to protect yourself:

- "When you buy a tax sale property, prepare to own it for at least a year. And hedge yourself to avoid losing it to the right of redemption."
- Use public data to understand some of the owner's circumstances. This will help you greatly reduce your risk:
    - Are they local?
    - Did they live in the property within the last few months before the sale? (If they didn't and you can prove it, they can't claim it back).
    - What's their debt situation?
- The best way to squash this problem? Locate the owner and have him/her sign a quit claim deed.

JumpStep 2 *(continued)*
Source a Property

2.3 Agreement of Sale

Once you've found your property and make an offer, be sure to ***read your AOS (Agreement of Sale)***

- key protections are within the AOS:
    - mortgage contingency
    - inspection contingency
    - zoning contingency
    - environmental contingency

HOMEWORK

USING WHAT YOU NOW KNOW

Take Action

- [ ] Read the glossary of real estate terms, and make sure you understand them. Circle the five terms you're least familiar with.
- [ ] Fill in the "real estate acronym" worksheet (on the next page)
- [ ] Join your local Jumpstart Facebook group
- [ ] Join your local Jumpstart Developers' Network

Read

- [ ] "What to Look for at a Sheriff Sale"

Research

- [ ] Research local neighborhood associations (compile a list and read their newsletters/ blogs/Facebook pages)
- [ ] Contact other real estate and development networking groups
- [ ] Find three potential properties using the property sourcing tools

Write

- [ ] Write down the one thing you learned in Session 1 that surprised you the most. (Be prepared to share it in Session 2.)

WORKSHEET

REAL ESTATE DEVELOPMENT ACRONYMS

Fill in the words for each acronym, based on the definition.

1. APR A.................................... P.................................... R....................................

The actual effective rate of interest charged on a loan expressed on a yearly basis. It represents the full cost of all elements associated with obtaining a full mortgage into a single formula. It is useful for comparing mortgage products.

2. ARM A.................................... R.................................... M....................................

A type of mortgage in which the interest rate applied on the outstanding balance varies throughout the life of the loan.

3. CO C.................................... of O....................................

A document that local government issues, stating that a building complies with building codes and laws and is in suitable condition to be occupied.

4. DSCR D.................................... S.................................... C.................................... R....................................

The ratio of cash available for repaying interest, principal, and lease payments of debt. To calculate, divide the net operating income (NOI) by the annual debt. Also known as DCR (Debt Coverage Ratio).

5. EGI E.................................... G.................................... I....................................

The amount of income a piece of property produces, less vacancy costs and collection losses. (For example, if an apartment complex has an income of $500,000 [if all units are rented], but historically, 20% of its units are left vacant, then its vacancy costs are $100,000 [$500,000 x 20%] and its EGI is $500,000 [minus] $100,000, or $400,000.)

6. LTC Ratio L.................................... to C.................................... Ratio

The loan percentage or amount a lender is willing to finance, based on the costs on the construction budget. Calculated from dividing loan amount by total costs (i.e., $160,000 loan / $200,000 budget = 80% LTC).

7. LTV Ratio L.................................... to V.................................... Ratio

The amount borrowed in a loan relative to the value of the property. (An LTV of 85% means the loan is for 85% of the value of the property, with the borrower making a down payment of 15%.)

8. NOI N.................................... o.................................... I....................................

A calculation used to analyze real estate investments that generate income: all revenue from the property minus all operating expenses. This is the income of a business (or individual) before taxes.

9. ROI R.................................... o.................................... I....................................

A performance measure used to evaluate the efficiency of an investment. It measures the return of an investment relative to the investment's cost. ROI = (Gains from Investment [minus] Cost of Investment) [divided by] Cost of Investment

QUIZ

WHAT YOU LEARNED IN SESSION 1

1. Investing in real estate:
   - ☐ **a.** is for everyone.
   - ☐ **b.** is a good idea if you have a high risk tolerance.
   - ☐ **c.** is a good idea only if you have an experienced partner.

2. Which strategy will best help you manage your level of risk in changing economic conditions?
   - ☐ **a.** Emphasize appreciation over cash flow.
   - ☐ **b.** Focus on cash flow over appreciation.
   - ☐ **c.** They're both equally useful.

3. The Jumpstart philosophy about sharing information with other developers is:
   - ☐ **a.** Be careful—we're all competing over the same piece of the pie.
   - ☐ **b.** Collaborating and sharing helps to grow the development pie so we can each have a bigger piece.
   - ☐ **c.** We should be part of the 80 percent that shares, instead of part of the 20 percent that does not.

4. Which two real estate sourcing strategies will work best for you?

SESSION 2

Contents

At the end of Session 2, you'll...

1. develop ***skills***
    - determine feasibility of a project
    - develop a design
    - create a scope of work

2. gain ***knowledge***
    - short and long-term strategies for reducing equity invested by refinancing
    - the basics of permitting and code considerations

3. obtain ***tools***
    - development Budget spreadsheets (for Buy & Hold/Buy & Sell)— available online
    - Pro Forma Profit & Loss spreadsheets (for Buy & Hold/Buy & Sell)—available online

JumpStep 3
Do Your Due Diligence

3.1 Consider ***all*** possible strengths, weaknesses, and liabilities of property purchase

Property factors—Take off the rose-colored glasses and identify all potential problems.

- Condition: What shape is it in? Are there structural issues?
- Use
- Layout
- Environmental assessments
- Code/zoning restrictions

Financial factors—Don't make assumptions. As much as possible, quantify all risks.

- What are the construction costs?
- What will be your operating costs?
- What rents are possible? Be conservative!
- What is the property value after stabilization?

What's your game plan for the property? Rent/Sell/Live? Gut rehab/cosmetic changes?

TIP: Hire a contractor to examine the property to point out deficiencies and provide a construction estimate.

TIP: Hire a home inspector for your first three projects. Follow the inspector around the house and take notes! You won't need a home inspector for your fourth project. By then, you'll know what to look for.

3.2 Find out the zoning classification

- Be sure you know what you're buying. Ask: "What does the current zoning allow? Is the current use legal?"
- Determine the zoning of the property using the city/town website. The zoning code will describe what is allowed in each specific zoning designation. For example, if a property is zoned commercial, you might not be able to legally use the first floor for residential without a zoning variance (exception).
- If zoned incorrectly for your proposed use, get zoning approval before purchasing and/or beginning construction.
- If a variance is needed, the process includes applying for a zoning permit, getting refused, and appealing the decision to the zoning board. Remember to factor in the time and cost of this process. If the property is owned by an LLC, you'll need to hire an attorney to represent you.

TOOL 3.1

AN INTRODUCTION TO RESIDENTIAL ZONING

(based on a handout from Steve Masters, Esquire, Just Laws PLLC)

When am I required to get Zoning approval?

Zoning is one of the first steps in the development approval process. Each land use activity must demonstrate that it conforms with the municipality's zoning laws—whether it's simply a change in land use, brand new construction project, or rehabilitation project.

Zoning regulations ensure that the land use, site layout, and building on every parcel of land are compatible with its surrounding conditions.

Will I need a Zoning Permit?

Generally, a project will need a new zoning permit if it involves:

- changes in use
- new construction or additions
- alterations that result in a change in gross floor area
- carports, detached private garages, greenhouses, and rear yard sheds (for homes above a certain size)
- installation of a fence (if it exceeds the height limits the zoning code establishes)
- construction of a deck higher than a certain height
- wind energy conversion systems or ground-mounted/freestanding solar collectors
- creation of off-street parking or reconfiguration of existing parking
- changes to a property's zoning classification ("zoning map revision")

TOOL 3.1 (CONTINUED)

AN INTRODUCTION TO RESIDENTIAL ZONING

(based on a handout from Steve Masters, Esquire, Just Laws PLLC)

Who can apply for zoning approval?

Property owners may file a zoning application, as well as agents of the property owner authorized in writing (such as tenants, family members, attorneys, licensed architects, licensed engineers, licensed contractors or licensed expeditors).

Check for:

- allowed ***uses and dimensional standards*** for the base zoning district.
- ***development standards***, such as: form and design, landscape, trees, outdoor lighting, fencing, historic preservation, parking, and signage requirements.
- ***overlay zoning*** district requirements. (An "overlay district" is superimposed on a base district and modifies or supplements the base zoning regulations.)

Access Philadelphia's Zoning Code at http://www.phila.gov/li/Pages/Zoning.aspx

Using the Zoning Code

There is a useful quick guide to the Philadelphia Zoning Code at http://www.phila.gov/CityPlanning/resources/Publications/Philadelphia%20Zoning%20Code_Quick%20Reference%20Manual.pdf

1. Look up the base and overlay districts that apply to the subject property. (Access Philadelphia's online zoning map at http://gsg.phila.gov/map)
2. Determine if the proposed use is permitted in the base district by reviewing the applicable ***Use Tables*** for the proposed use. (Consult §14-602 of the Philadelphia Zoning Code.)
3. Review ***Dimensional Tables*** to see the permissible lot area, lot width, open area, building height, setbacks, and/or gross floor area for the district. (Consult §14-701 of the Philadelphia Zoning Code.)
4. Determine the requirements for vehicle and bicycle ***parking***, as well as off-street ***loading***. (Consult §14-800 of the Philadelphia Zoning Code)
5. Review any sign requirements. (Consult §14-900 of the Philadelphia Zoning Code)
6. Beware of requirements in a historic district or for a historic property.

Permits: How do I get zoning approval?

If zoning approval is needed, there are four main paths to getting a zoning permit in Philadelphia:

- by ***right/as-of-right***. When the project proposal complies with all zoning provisions applicable to the property, an applicant can get a zoning permit from Licenses and Inspections (L&I) "by-right" without any action by the Zoning Board, Planning Commission, or City Council. Certain large projects must go through an advisory Civic Design Review process.
- by qualifying as a ***nonconforming*** use. Many land uses, buildings, parking areas, lots, signs, and site improvements in the City were established before the adoption of zoning, or they were legal when established but have become nonconforming due to later zoning changes. The Zoning Code regulates the continued existence, use, modification, and expansion of these nonconformities. (Consult §14-305 of the Philadelphia Zoning Code for addition information.)
- by ***special exception***. The Zoning Code permits certain uses and development by special exception, which is granted by the Zoning Board if the project is compatible with the surrounding neighborhood.
- by ***variance***. Sometimes special circumstances prevent projects from conforming to the Zoning Code standards. In these instances, applicants must obtain a variance from the Zoning Board to deviate from the zoning standards. The Zoning Board will verify that there are special circumstances presenting an unnecessary hardship in complying with the Zoning Code.

An application for a variance or special exception will require ***neighborhood meetings*** with Registered Community Organizations (RCOs) and then approval by the Zoning Board of Adjustment.

JumpStep 3 *(continued)*

Do Your Due Diligence

3.3 Develop a list of "comps" (comparable properties in the area)

Use properties that have sold or rented over the past 12–18 months. Go to open houses and review MLS, Zillow, or similar databases to help develop your list of comps.

Include:

- address
- actual sales/rent price
- date sold/rented
- square feet
- # of bedrooms & bathrooms
- amenities such as finished basement or deck

TOOL 3.2

SAMPLE LIST OF "COMPS"*

COMPARABLES				
ADDRESS	PROPOSED SALE PRICE		SF	BR/BA
Subject Property	$250,000		1,550	3/2
SALE VALUE				
ADDRESS	SALE PRICE	DATE SOLD	SF	BR/BA
375 N Main St	$253,000	7/13/2016	1,600	3/2
345 N 1st St	$230,000	11/14/2016	1,312	3/1.5
280 N East St	$270,000	11/7/2016	1,620	3/3
401 N East St	$339,000	2/5/2017	1,800	4/2
RENTAL VALUE				
ADDRESS	RENT	DATE RENTED	SF	BR/BA
350 N Main St	$1,500	1/12/2017	1,200	2/1
400 N 3rd St	$1,600	4/15/2017	1,300	2/2
550 N East St	$1,750	5/10/2017	1,475	3/1
Zillow estimate for property	$1,700		1,550	3/1
Rent-o-meter for property	$1,610		1,550	2/2

* These locations and values are for educational purposes only.

JumpStep 3 *(continued)*

Do Your Due Diligence

3.3 Determine financial feasibility

- Fill out a development budget for your project
  - Acquisition costs
  - Construction costs
    - Include 15% contingency for rehabs
    - Include 5% contingency for new construction
- Complete profit and loss statement
  - for Buy and Hold: expected ROI? Consistent with risk taken?
    - DCR (Debt Coverage Ratio) of 1.25 or higher?
  - for Buy and Sell: 20% or higher net margin?

TIP: These budgets are available as Excel spreadsheets on the Jumpstart website (www.gojumpstart.org).

TIP: When you plug in rent values, subtract 10% for vacancies and bad debt.

TOOL 3.3

PRO FORMA: BUY AND HOLD PROFIT AND LOSS

*Only complete this statement if you are planning to **hold** the property.*
Download the Excel version at www.gojumpstart.org

PURCHASE

PROPERTY COSTS	
Purchase Price	$82,000
Construction Costs	$25,300
Total	**$107,300**

PERMANENT BANK LOAN	
LTV	85%
Amount	$91,205
Rate	5.00%
Term	25 years

ASSUMPTIONS
1. 4-month rehab
2. 3BR / 2 bath
3. Tenant pays all utilities
4

INITIAL INVESTMENT	
Down payment @ 15%	$16,095
Settlement Costs @ 5%	$4,100
Financing Costs @ 2% + $250 +$1,500	$3,644
Holding Costs (utilities, taxes, insurance)	$600
Other?	$
Total	**$24,439**

RENTS (MONTHLY)	
Tenant No. 1	$1,350
Tenant No. 2	$
Tenant No. 3	$
Total	**$1,350**

OPERATING BUDGET

3%=annual rent increase; 3%=annual expense increase

YEAR NO.	1	1	2	3	4	5	6	7	8	9	10
	2016 Annual	2016 Monthly	2017	2018	2019	2020	2021	2022	2023	2024	2025
REVENUE											
Gross Income	$16,200	$1,350	$16,686	$17,187	$17,702	$18,233	$18,780	$19,344	$19,924	$20,522	$21,137
Less Vacancy @ 10%	($1,620)	($135)	($1,669)	($1,719)	($1,770)	($1,823)	($1,878)	($1,934)	($1,992)	($2,052)	($2,114)
Effective Gross Income	**$14,580**	**$1,215**	**$15,017**	**$15,468**	**$15,932**	**$16,410**	**$16,902**	**$17,409**	**$17,932**	**$18,470**	**$19,024**
OPERATING EXPENSES											
Management Fees @ 6%	$875	$73	$901	$928	$956	$985	$1,014	$1,045	$1,076	$1,108	$1,141
Insurance	$952	$79	$981	$1,010	$1,040	$1,071	$1,104	$1,137	$1,171	$1,206	$1,242
Real Estate Taxes	$2,320	$193	$2,390	$2,461	$2,535	$2,611	$2,690	$2,770	$2,853	$2,939	$3,027
Alarm Monitoring	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Repairs	$1,000	$83	$1,030	$1,061	$1,093	$1,126	$1,159	$1,194	$1,230	$1,267	$1,305
Trash Removal	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Lawn Care & Snow Removal	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Water & Sewer	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Gas & Electric	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Rental License	$50	$4	$52	$53	$55	$56	$58	$60	$61	$63	$65
Total Operations	**$5,197**	**$433**	**$5,353**	**$5,513**	**$5,679**	**$5,849**	**$6,025**	**$6,205**	**$6,391**	**$6,583**	**$6,781**
PROFITS											
Net Operating Income	**$9,383**	**$782**	**$9,665**	**$9,955**	**$10,253**	**$10,561**	**$10,878**	**$11,204**	**$11,540**	**$11,886**	**$12,243**
Debt Service	($6,398)	($533)	($6,398)	($6,398)	($6,398)	($6,398)	($6,398)	($6,398)	($6,398)	($6,398)	($6,398)
Net Cash Flow	$2,985	$249	$3,267	$3,557	$3,855	$4,163	$4,480	$4,806	$5,142	$5,488	$5,845
Debt Coverage Ratio	1.47		1.51	1.56	1.60	1.65	1.70	1.75	1.80	1.86	1.91
Return on Investment	12.21%		13.37%	14.55%	15.77%	17.03%	18.33%	19.67%	21.04%	22.46%	23.92%

TOOL 3.4

PRO FORMA: BUY AND SELL PROFIT AND LOSS

*Only complete this statement if you are planning to **sell** the property.*
Download the Excel version at www.gojumpstart.org

GROSS SALES REVENUE	
Expected Listing Price	$220,000
Realistic Sales Price	**$210,000**

PURCHASE AND REHAB

ACQUISITION & CONSTRUCTION COSTS	
Purchase Price	$103,000
Settlement Costs @ 5%	$5,150
Construction Costs	$34,040
Total	**$142,190**

CASH NEEDED	
Developer's Equity @ 15%	$21,329
Administration Fee	$1,500
Holding Costs (utilities, taxes, insurance)	$1,000
Total	**$23,829**

JUMPSTART GERMANTOWN LOAN	
LTV	85%
Total Project Cost	$120,862
Financing Fee @ 2%	$2,417
Legal Fee	$250
Loan Amount	**$123,529**
Rate	6.75%
Term	Interest only

NET PROFIT ON SALE

REVENUE	
Selling Price	$210,000
Settlement Cost Upon Sale @ 2%	($4,200)
Sales Commission @ 6%	($12,600)
Gross Profit	**$193,200**

EXPENSES	
Acquisition and Construction	($142,190)
Holding Costs	($1,000)
Interest on Loan	($3,127)
Total	**($146,317)**

PROFITS	
Net Profit	**$46,883**
Net Margin on Sale	**24.27%**

ASSUMPTIONS
1. Interest on loan calculated for 9 months at 50% ramp up
2.
3.
4.
5.

JumpStep 4
Find Your Financing

4.1 Identify funding sources

For equity in/down payment

- Borrow from family or friends
- Take out a line of credit on your home
- Find an investor or partner
- Crowd funding

Loans available

- Nontraditional funders
  - Jumpstart Loan Program (if available in your neighborhood)
  - Hard money lenders
- Government or Traditional Loans
  - Financial institutions/banks
  - Credit unions
  - CDFIs (Community Development Financing Institutions)
  - Local or state government loan programs
- Get creative!

4.2 Secure a loan

- Bankers are not scary people! Your earnestness and goodwill go a long way. Most lenders will be willing to go step by step with you—especially a credit union or CDFI.
- Be prepared! Review the list of items you'll need for a loan application (see **TOOL 4.1** on next page) and assemble them ahead of time.
- Be organized and professional in your presentation and know the real estate lingo. This will get you the respect you need to overcome your initial lack of experience!
- Follow through—don't drop the ball.
- Get involved with appraisals.
  - Meet appraisers at the property and feed them the info they need.
  - Feel free to appeal an inaccurate appraisal. Appraisals can be way off, especially if the appraiser does not know or understand the neighborhood.
- Remember: Everything is negotiable.
  - If the bank offers you an interest rate of 5%, ask for 4.75%!
  - Or better yet: get bids from three different banks, and play them against each other.

TOOL 4.1

BASICS YOU NEED FOR A BANK LOAN APPLICATION

(Adapted from a list supplied by William Pounds, Senior Vice President and Director of Commercial Real Estate, Republic Bank, February 2017.)

1. Copy of ***driver's license***
   (or passport or official ID)
2. Two (2) most recent years completed ***Federal Tax Returns*** (signed).
   Include any extension requests (if applicable)
3. Current Personal ***Financial Statement*** (signed).
   Should be less than six (6) months old
4. If titled in an Entity (LLC, LP, S CORP):
   Two (2) most recent years completed ***Entity Federal Tax Returns*** (signed);
   include any extension requests (if applicable)
5. Copies of ***bank statements***
   to support any liquidity you noted on your personal financial statements
6. Copy of ***organization documents***:
   Partnership Agreement, Operating Agreement, Certificate of Formation (for LP or LLC),
   Articles of Incorporation and Bylaws, Tax ID Number
7. Copy of ***Lease(s)*** (if applicable)
8. ***Agreement of Sale*** (if applicable)
9. ***Construction Budget*** (if applicable)
   (see JumpStep 5.1)
10. ***Pro forma***
    operating statement for rental, plus information about any historical income and expenses.
    (Include comparable rents in the area to support your rent estimate.) (see JumpStep 3.4)
11. ***Comparable sales*** in area
    to support your expected sales price (if applicable; see JumpStep 3.3)
12. ***Resume*** of professional experience

JumpStep 4 *(continued)*
Find Your Financing

- Become familiar with general terms for commercial loans
    - Loan to Value Ratio: Typically 75% LTV
    - Loan to Cost for Renovation Loan: Typically 80% LTC
    - Minimum Debt Service Coverage Ratio: Typically 1.25x
    - Amortization:
        - Either 20 or 25 years
        - Balloon: 5 years
        - Recourse: Personal Guaranty Required

4.3 Your long-term real estate investment strategy for buy and holds

Once you've purchased and stabilized one or more properties, you want to refinance that asset so you can buy more. BRRRR (Buy; Renovate; Rent; Refinance; Repeat) is a way to get more capital out of your projects sooner.

TOOL 4.2

"BRRRR" STRATEGY: BUY; RENOVATE; RENT; REFINANCE (AND REPEAT!)

1. ***B*uy**
   Purchase a house that needs TLC for $50K!

2. ***R*enovate**
   Provide that TLC, along with some dollars (let's say $25K).

$50K	*Acquisition costs*
+ *$25K*	*Construction costs*
$75K	*Total Acquisition & Construction costs*

3. ***R*ent**
   Place happy tenants in your new house and earn rent.

4. ***R*efinance**
   After all your hard work, your house is now worth more because it has been rehabbed and fully rented! Let's say the new appraised value of your rental property is $120K. Cash out refinance at 75% LTV, to pull $90K in equity from the house and pay off $75K acquisition and construction loan.

$90K	*Cash out refinance*
– *$75K*	*Pay off Acquisition & Construction costs*
$15K	*Cash out*

5. ***R*epeat**
   Follow this same strategy with your next property and refinance every five years if the property value has gone up significantly. Your goal should be to have negative equity in your project.

JumpStep 5
Develop Design & Procure Permits

5.1 Create a scope of work

A house/apartment is only as good as its worst feature! Look at the property as if you are a potential homebuyer or tenant.

Spend a couple of hours in the house/apartment(s) to develop a detailed scope of work. The scope should include:

- as much detail as possible
- number of items to be repaired/replaced (i.e. windows, doors)
- square footage of floors to be repaired/replaced
- level of desired finishes (i.e., builders' grade kitchen cabinets, granite countertops)
- a list of unknowns that need further investigation (i.e., operability of heater, life of roof)

A vague or incomplete scope of work is a surefire way to lose money! (See **TOOL 5.1** on next page.) Hand your scope of work to contractors to obtain a price for your exact specifications so you get comparable estimates from each contractor.

TIPS:

- Record all the ideas and suggestions contractors offer!
- Always install double-paned windows if they do not currently exist in the house/apartments. They will reduce your tenants' utility costs and buyers will demand them.
- If you finish the basement with walls, floors, etc., installation of a French drain is a must to protect your investment against moisture/water penetration.
- Ask your contractors to provide you with an estimate based on your scope of work. If the contractor wants to offer more or fewer items to his/her estimate, they can provide "alt adds" or "alt subtracts" for you to consider.

TOOL 5.1

HOW TO WRITE A SCOPE OF WORK

Project Scope of Work

The work shall include, but not be limited to, all labor, materials, tools, equipment, incidentals, insurance, overhead, permits, and profit to perform the work as outlined below:

General notes:

1. Contractor has inspected and accepts all surfaces and job conditions. Costs associated with these conditions are included within this proposal.
2. Contractor shall field verify locations, sizes, and quantities of work required for the project.
3. Include all required cleanup for work completed under this scope. Contractor will include daily cleanup of all areas where work is performed and prompt disposal of debris.
4. Contractors shall be responsible for all permits and licensing, as required.
5. Contractor shall provide proof of General Liability and Worker's Compensation insurance.

Owner Furnished vs. Contractor Furnished Material Designation

OFCI—Owner Furnished, Contractor Installed.

CFCI—Contractor Furnished, Contractor Installed.

A. Demolition

1. Remove stairwell/kitchen partitions on main level. Temporarily shore ceiling as necessary.
2. Remove walls around staircase to create open stairs. Temporarily shore ceiling as necessary.
3. Remove existing kitchen cabinets.
4. Remove existing gyp board bulkheads & soffits.
5. Remove existing light fixtures.
6. Disconnect/cap plumbing for kitchen sink.

B. Drywall/Carpentry/Insulation (CFCI unless noted)

1. Furnish and install new structural beam between kitchen/stairwell.
   Shore existing ceiling as required to install beam and remove structural walls.
2. Construct half-wall partition (4ft tall) at stairs.
3. Infill existing exterior door with framing, drywall & batt insulation.
   Siding patching in siding scope of work.

4. Infill existing door opening between dining room and master bedroom.
   Patch bedroom side with salvage wood paneling.
5. Patch ceilings as required where soffit is removed.
6. Install kitchen cabinets per the layout shown.
7. Install countertops and sink. (OFCI)
8. Install crown molding, base molding, filler panels, end panels, & trim pieces.

C. Plumbing (CFCI unless noted)

1. Remove any existing piping as required to complete new plumbing work.
2. Remove existing galvanized waste lines at existing kitchen sink & replace w/ PVC.
3. Provide rough-in for new kitchen layout.
4. Provide water supply and new waste lines to sink.
5. Install new kitchen faucet. (OFCI)
6. Install new garbage disposal and connection to dishwasher discharge. (OFCI)
7. Provide & connect water supply to dishwasher.
8. Provide & connect water supply to refrigerator.
9. Remove and cap existing gas service line to kitchen.

D. Electrical (CFCI unless noted)

1. Replace existing electrical panel with new 200 AMP panel & circuit breakers.
2. Rough-in new power & lighting for kitchen as required by code.
   a. Install new GFI protected outlets along new kitchen cabinet layout as required by code.
   b. Install new outlets for appliances as required.
   c. Install (04) new can lights. (OFCI)

TOOL 5.2

SAMPLE CONSTRUCTION BUDGET*

CONSTRUCTION COSTS	
Demolition	$5,000–$7,000
Drywall	$2,000–$4,000
Carpentry	$2,000–$4,000
Insulation	$1,000–$3,000
Plumbing	$6,000–$8,000
Electrical	$8,000–$10,000
Other	$0
Subtotal	$24,000–$36,000
15% Contingency	$3,600–$5,400
Total Construction	**$27,00–41,400**

* These amounts are for sample purposes only and do not necessarily reflect amounts for accurate estimating.

JumpStep 5 *(continued)*

Develop Design & Procure Permits

5.2 Understand the 3 levels of renovations

A municipal department of licenses and inspections will require permits depending on the extent of your renovations.

- ***level 1: minimal***
  - minor removal/replacement of existing materials, coverings, equipment, plumbing, fixtures
  - May need permit (can possibly obtain online)
- ***level 2: moderate***
  - reconfigure the existing space; add or eliminate windows or doors; expand the mechanical or plumbing systems
  - need permit
- ***level 3: gut rehab (50–100% of the property)***
  - altering the structure; change a load-bearing wall
  - Need permit and professional services (and drawings): structural engineer or architect

JumpStep 5 *(continued)*
Develop Design & Procure Permits

5.3 Determine what approvals you need

- Local department of licenses and inspections
    - zoning permit
    - use registration permit
    - building permit
- Special approvals (possibly needed)
    - Historic Commission
    - Art Commission
    - Zoning Board
    - City/town Council
    - Water Department
    - Planning Commission
    - Streets Department
- When the city/town will inspect
    - pre-project: walk-through just before you start
    - after demolition
    - before/after you pour foundations
    - rough framing (with mechanical, electrical exposed), before you close walls and drywall
    - final walkthrough to get CO (Certificate of Occupancy)

TIP: Perform construction in the correct order. Find out when the city/town wants their next inspection so you're prepared. You want to avoid having to take down drywall you just put up.

HOMEWORK

USING WHAT YOU NOW KNOW

Take Action

- [ ] Download the following Excel spreadsheets from the Jumpstart website (www.gojumpstart.org)
  - Pro formas (Buy and Sell, Buy and Hold)
  - Development budget
- [ ] Visit a property for sale and complete a development budget and pro forma for that property.

Watch

- [ ] Prepare for the Site Visit (in Session 3) by watching (on the Jumpstart website) a video about a property located in the Fairmount section of Philadelphia (7.5 minutes).

Read & Review

- [ ] **TOOL 3.1:** "An Introduction to Residential Zoning"
- [ ] **TOOL 3.2:** "Sample List of Comps"
- [ ] **TOOL 3.3:** "Pro Forma: Buy and Hold Profit and Loss"
- [ ] **TOOL 3.4:** "Pro Forma: Buy and Sell Profit and Loss"
- [ ] **TOOL 4.1:** "Basics You Need for a Bank Loan Application"
- [ ] **TOOL 4.2:** "'BRRRR' Strategy: Buy; Renovate; Rent; Refinance; Repeat"
- [ ] **TOOL 5.1:** "How to Write a Scope of Work"
- [ ] **TOOL 5.2:** "Construction Budget"

QUIZ

WHAT YOU LEARNED IN SESSION 2

1. What is the best way to build a repeatable investment model that works for you?

- [ ] **a.** BRRRR (Build Reserves for Rapid Repeated Returns): Your investment power is limited to your savings. Save as much money as you can so you always have funds for the next deal.
- [ ] **b.** BRRRR: Avoid cold-weather markets and only invest in hot neighborhoods. Consider vacation rentals in Florida!
- [ ] **c.** BRRRR (Buy; Renovate; Rent; Refinance; Repeat): Look for opportunities to improve property value and refinance to get your initial investment (and more) back.

2. When completing a pro forma: (Select all that apply)

- [ ] **a.** Be conservative. Protect yourself against worst-case scenarios by basing your decisions on the lowest income and highest expenses reasonably possible.
- [ ] **b.** Be optimistic! Always put the highest income and lowest expenses possible. You don't want to talk yourself out of a deal you like, and what your lender doesn't know won't hurt them.
- [ ] **c.** Get multiple estimates from contractors as needed to complete your construction budget.
- [ ] **d.** Include, at least, a 15% contingency for construction.

3. True or False? You should ALWAYS:

T F Fall in love with your real estate

T F Form an LLC

T F Use Jumpstart Germantown as a resource through its Facebook page and Developers' Network

SESSION 3

Contents

At the end of Session 3, you'll...

1. develop ***skills***
    - choose a contractor
    - market a property

2. gain ***knowledge***
    - steps involved in residential rehab
    - how to attract and retain tenants

3. obtain ***tools***
    - tips for picking a contractor
    - writing a sample rental application
    - completing a residential lease

JumpStep 6
Customize Construction

6.1 Actively manage the construction process

- What's your passion? Providing good, affordable housing? Preservation of historic buildings? Tap into what inspires you.
- Be hands-on. Be prepared to put on your work gloves and borrow a friend's truck. You're the engine that keeps things moving.
- Over time, you want to build construction knowledge and capacity. Ultimately, you can develop a pipeline of projects, and assemble a small team of loyal people who can work independently and help you manage projects.

6.2 Working with contractors (see **TOOL 6.1**)

- union vs. non-union
- in-house (your own construction team) vs. out-of-house (subcontractors)
- negotiate and sign a construction contract (can use the scope of work)
- closely oversee your contractors
- handle unforeseen conditions, change orders, and problems

TIPS:

- Ask friends and colleagues for contractor recommendations.
- Go to Home Depot and strike up conversations with contractors. Ask for cards, visit job sites, and get pricing.
- Drive around and look for good work being done on other houses/apartments in the neighborhood.

6.3 Construction Timeline

- Do everything in the proper order.
- Hire a General Contractor (GC), project manager, or do it yourself.
- Watch the progression. It should go fast, but not too fast.
    1. Demo/Cleanout
    2. Framing
    3. Mechanicals
        - HVAC
        - Plumbing
        - Electrical
    4. Insulation
    5. Drywall
    6. Trim
    7. Paint
    8. Floors
    9. Punch-list
    10. Stage for sale or rent

6.4 Troubleshoot: When everything goes wrong

Keep calm and carry on. Solve one problem at a time, and resolve issues amicably and efficiently. Look for common ground with your contractor and "keep the peace." You want to establish a relationship with your contractor to use him/her over and over again.

TOOL 6.1
10 TIPS ON SELECTING A CONTRACTOR

Adapted from Joseph Scorese, "10 Tips on How to Hire a Contractor for Your House Flip," LinkedIn, January 23, 2016 (https://www.linkedin.com/pulse/10-tips-how-hire-contractor-your-house-flip-joseph-v-scorese).

Be picky and follow these guidelines:

1. Check references
Ask a contractor to show you his/her work. Or ask them for contact information for 3 to 5 recent clients (not from relatives!). Ask for "before and after" photos of their construction projects.

2. Get three bids
Ask the same list of questions of each contractor you interview. Don't automatically go with the lowest bid to save money—or assume the highest bid means higher quality and service. Remember, materials and labor have fixed costs, so be skeptical of any bid that's dramatically lower or higher than the others. Go with your gut—the winning bid should make sense to you and inspire your confidence in the contractor.

3. Compare "apples to apples"
All written bids must cover the EXACT same scope of work, so you can compare the quotes evenly. A contractor should leave nothing off, and if they want to add or subtract items, they must do so separately. Create an itemized spreadsheet to compare each contractor's bid.

4. Confirm they're licensed and insured
Don't only ask for proof—go one step further and verify the information they give you with your state or city's contractors' licensing board. It's the only way to ensure they're conducting business legally.

5. Interview them and trust your gut
Treat the meeting like a job interview. Evaluate their professionalism. Were they late? Were they rude over the phone? Prepare specific questions, and notice how thoroughly they address your concerns. Avoid anyone who makes you feel remotely uncomfortable. There are plenty of qualified contractors available.

6. Be specific about parameters and time frame

Communicate clearly about price, payment terms, and job schedule (when the project starts, working hours, number of days per week they will be on site). Write into the contract a penalty if they don't complete work on time (e.g., deduct $50–$100 from the price for every day past the scheduled completion date). This should be standard operating procedure for experienced, quality contractors who do flips or tenant rehabs.

7. Be clear on the payment schedule

Have the contractor agree to the payment terms in writing. Cover circumstances such as who is providing materials or the process for approving change orders. If possible, do not pay upfront or ahead. Pay only for work that has been completed.

8. Make sure their expertise fits

Just because a contractor did a great job on a friend's house doesn't mean they're right for your project. If you need doors and windows installed, then you can't rely on a contractor whose only references are for plumbing and electrical jobs.

9. Check if you need a permit

Be wary of contractors who try to convince you that you don't need a permit for a project. They should help you navigate the process—not be someone you have to second guess. Research permit requirements in your area and confirm with development colleagues or a local architect whether a permit is needed before proceeding.

10. Don't rush into anything

Renovations can be exciting but be cautious and patient. Always do your due diligence—it will pay off in the end!

JumpStart 7
Lease/Manage/Sell Your Property

7.1 Marketing to lease your property

A. Finding tenants

- Walk the unit

  Think about whom you're looking to attract and put yourself in their shoes. Place unique elements into the listing. Be honest and accurate. Sell the space.

- Advertising

  You want exposure to build a pool of good applicants. It's a "volume" game.

  - List the property online—use a descriptive tagline. Craigslist is still effective. Look at other ads for ideas and competitive advantages.
  - Use lawn signs, banners, and flyers.
  - Ask the neighbors to suggest potential tenants.

- Showings

  Hold open houses—they're more efficient and effective!

  - Host several open houses, to accommodate peoples' schedules.
  - Make open houses 1 hour long, on an evening or weekend.
  - Get to know potential tenants and what they're looking for. Begin to evaluate whether they will be good long-term tenants. Find out: What is the tenant's story?
  - Move and respond quickly. Call prospective tenants back right away and aggressively follow up. It will increase your chances of renting quickly.

B. The application process: Getting to "yes"

Applicants have lots of housing choices. Make the process easy and simple!

A sample rental application is available at gojumpstart.org.

C. What makes a good prospective tenant? Someone who:

- is ready to move in right away
- has a credit score of 700 or more
- has a monthly income of at least 3x the listed rent (preferably 4x)
- shows concern about the condition of the house/apartment
- has a history of staying several years in previous rentals
- has a stable work history.

D. Tenant application ***Dos*** and ***Don'ts***

- ***Do*** require:
  - work history (previous 3 years)
  - rental history (previous 3 years)
  - reference(s) from previous landlord(s)
  - first month's rent, last month's rent, and at least one month's security deposit
- ***Do*** run a credit check once you've identified them as a desirable tenant.
- ***Do*** have a conversation with the prospective tenant: Reasons for moving? Expected length of stay?
- ***Don't*** bother with application fees. They discourage tenants from applying, which may net you fewer choices.
- ***Do*** adjust your strategy based on the size of your applicant pool.
  - large pool: Be choosy!
  - small pool: Consider less-qualified tenants.
- ***Do*** negotiate multi-year leases, if possible.

7.2 Marketing to sell

- Decide whether to ***sell the property yourself***, or ***hire a broker***.
- Are ***current tenants*** interested in buying?
- Ask ***neighbors*** if they know anyone interested.
- Are there ***comparable houses*** on the market? If so, price your house/apartment accordingly. Provide similar amenities.
- Advertise.
- Stage the unit/property.

JumpStart 7 *(continued)*

Lease/Manage/Sell Your Property

7.3 Leasing and managing your property

The best way to increase your cash flow and ROI is to reduce tenant turnover by retaining good tenants. Keeping your units rented throughout the year is the best way to turn a measly 5% return into a 15%, or more, annual profit.

<u>Option 1: Use a property management company</u>

- They'll ***find tenants***, ***collect rents***, and/or perform ***maintenance and repairs***.
- They'll charge ***6–10% of the rent*** collected.
- ***Get recommendations*** before you hire.
- ***Meet with them once a month*** to stay up to date and keep them motivated.
- ***Consider a hybrid plan***, where you share management responsibilities so you can do what you do best and enjoy most.

<u>Option 2: Manage the property yourself</u>

If you have time, no one can manage the property like you—the owner—can. You'll be more aggressive and your property will see a better ROI.

A. ***Write a lease***
- Find a lease template that includes all necessary legal language, through:
  - an office supply store, like STAPLES®
  - a realtor you know
  - a state realtors' association (e.g., https://eforms.org/rental/pa/pennsylvania-association-of-realtors-residential-lease-agreement/)
  - add in your own rules and regulations

B. ***Obtain appropriate licenses***

To collect rent, municipalities may require a:
- "commercial activity" license (In Philadelphia this is a one-time, free license that you can obtain online)
- rental license (one per unit, usually includes a fee, renew annually*)
- "rental suitability certificate" (one per each individual tenant, must reapply when a new tenant moves in)

C. ***Provide the tenant with documents that are required by law:***
- State-produced booklet summarizing your responsibilities as a landlord
- Certificates pertaining to use of lead-based paint (if there will be children under 6 years of age living in the unit); these require property inspections and a fee*

* Remember to include these costs in your pro forma!

A few things to remember about managing a property:

- ***Communicate*** with your tenants. A happy tenant is a good, long-term tenant.
    - Don't get behind on repairs.
    - Keep tenants informed.
- ***Utilities***: Separate utilities by unit, when possible, so tenants have an incentive to monitor and limit their utility use.
- ***Rent collections*** and accounting: use standard computer-based systems like QuickBooks, or look into a cloud-based system like AppFolio.
- ***Overdue rent***
    - Be consistent and fair to your tenants.
    - Have a clear internal policy on overdue payments (e.g., file for eviction when tenant becomes 2 months delinquent).
- ***Evictions***
    - Evictions can take 3–4 months, not including tenant appeals.
    - It's worth hiring an attorney to help you.
    - You're required to store the belongings of the evicted tenant under state law (approximately 30 days).
- ***Raising the rent***: factors to consider
    - How often? How much?
    - How will increases affect turnover?
- ***When a tenant leaves***
    - Stick to the terms in your lease about giving advance notice on showing the unit to other prospective tenants.
    - Use your existing tenant to help you find a new tenant.
    - You have 30 days to return the security deposit, or put in writing to them why you're not returning it.

ACTIVITY

REVIEWING WHAT YOU'VE LEARNED

Grab a partner and review what you learned from this session by answering a few questions:

True or False? (Circle one)

You should ***always***:

1. T F Verify that zoning is correct for your intended use
2. T F Carry builders risk insurance
3. T F Pay your contractor a large deposit up front
4. T F Check your contractor's license and insurance
5. T F Pull construction permits
6. T F Obtain Housing Inspection & Rental Suitability Licenses

Fill In

7. What are the stages of construction when city officials will inspect your construction project?

....

....

8. What are some strategies for property management and leasing that will help you keep your vacancies low and turn units over quickly?

....

....

Moving Forward

Now you're ready to pull it all together and take development to the next level!

1. Use your mentor effectively

Don't go it alone! Take your mentor/partner/contractor with you to look at a property.

Ask them: Is there too much risk? Does this project make sense?

2. Expand your capacity

- use other peoples' money (leverage resources, get bank loans, add investor capital)
- seek staff (for book keeping, back office support, etc.)
    - make your expectations clear
    - let them do their jobs
    - keep overhead relatively low
    - don't "feed the monster"
- use your time efficiently and effectively
    - multitask
    - write everything down
    - use email (rather than the phone) and social media
- find partners who have different skillsets than you

3. Pay it forward

- Gain enough experience so you're in a position to become a mentor.
- Be part of the 20% of real estate developers who share information and knowledge.
- Post resources on the Jumpstart Facebook page and use it to ask for help.

4. Make smart choices so you profit

Go forth and rehab! Follow your passion and enjoy what you do!

Notes

WWW.GOJUMPSTART.ORG

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