Urban Real Estate Development for Overseas Investors
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Presented by Steve Chianglin, Simon Malinowski, and Vince Sliwoski

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Vince Sliwoski 0:05

On the commercial real estate side, we have, we're also seeing a big spike in activity. Particularly over the last few quarters sales are now at pre pandemic levels fueled by historically low interest rates. But also just I think, a general belief by a lot of investors that the worst is behind us. Investors bought about almost $150 billion of us commercial property in the second quarter, that's literally three times the amount that was bought over the same quarter the year before during the pandemic, right. So in that sense, it's looking like a really fast rebound probably faster than after the global financial crisis of 2009. The market looks different than it did in March of 2020. certain cities like New York and San Francisco are rebounding but more slowly than really hot areas of the US like the Sunbelt. certain classes of properties are slower to come back, say downtown office buildings or convention hotels, other classes of real estate industrial weren't even affected really, by the pandemic and continue to sell very briskly. So that's kind of like big, big picture snapshot. The question really, after knowing all that is why why would you invest? Why invest in us commercial real estate? I think the first reason is just an obvious one is high income potential, right? with commercial and mixed use buildings in particular, you'll see higher rents, and price tags, and thus the potential for higher returns, you'll also see tax benefits, the US tax code is enormously favorable to real estate investors.

I'm just seeing a note you guys that there was a technical error with the webinar, and I'll have to start over, there was a technical error with a start. So I'm just going to get through this little part of the presentation, I'll reintroduce our firm, and we'll go from there. But I was saying that the tax code is enormously favorable, the commercial real estate investors. And that became even more true after the tax cut and jobs act as a few years back. What so advantageous about tax, there are a couple of big categories in my mind. First, you have something called depreciation. And that's the ability to book a loss in value of a property over the course of its useful life. So even if the property doesn't actually become less valuable, even if you wouldn't take a loss, if you sold it, you're still allowed to book a loss in value every year, over in the case of multifamily residential 27 and a half years, or over a 39 year schedule for commercial property. And when a property sold, the seller would in theory owe tax on the difference between the depreciated value and the sale price. We call that depreciation recapture. That's the point at which deferred taxes are supposed to be paid. But another big tax advantage is you can carry that property or put it into a light kind exchange, we call those a 1031. You've probably heard that term that allows a property owner including say an LLC, owned by multiple investors to sell a property and put that money into another property. If done within I think it's a six month period. So if that's done correctly, the owner pays no taxes on the same on the gain of the sale of the original building. So you've got depreciation, you have the ability to do 1030 ones, you have something called qualified business income deductions, which was a big change from the recent tax cut and jobs act that is basically an incentive for companies with a large number of employees, you would think it wouldn't apply to real estate investors. But during the tax bills negotiations in Congress, an exemption was added for real estate. So instead of considering employees for their deduction, real estate companies can use a different calculation based on their assets. So you've got TBI. And then there's all sorts of other small things like opera, it's not small, but new provisions for real estate investors like opportunity zones and other things that I won't get into in great detail. safe to say that it's a really nice tax environment for an asset class to invest in. And then you have things for individual investors to like estate planning benefits, the tax code is written just generally, so that the accumulated capital gains taxes are supposed to be paid eventually, right? But if an individual owns real estate properties can be held until death. At that point, all the embedded capital gains are wiped out, so no capital gains tax is owed. And the family inherits the properties that whatever value they were praised that on the date of death. So that's kind of big picture stuff. Those are generally applicable tax advantages to both residential and single family homes. The deduction some of the deductions went away. For instance, mortgage interest deductions and real estate tax interest deductions went away with respect to single properties, but I'd say it's still a very good tax environment.

Choices, us real estate investment options run the gamut. You can invest in things like a class, a office building, you could keep it small putting those dollars toward a single home or a storage facility or, I don't know, an industrial warehouse or a condo community, there's a lot of flexibility both in what you invest in and in where you can do it. Another reason people really like real estate investment is it's tangible, right? People understand it, a lot of people can understand real estate better than stocks because they grew up with it or real estate investing in their family or in their culture. I mentioned the superior tax benefits, I would say that real estate's interesting and attractive because it provides month to month cash flow if you rent it out. So you know, it's almost impossible to find a dividend paying stock that kicks out standard payments comparable to what you get in a standard triple net or other type of lease, I would argue that debt, or what we call leverage a lot in real estate is safer in the real estate, investment class. And with stocks in the simple reason for that is real estate prices don't fluctuate as widely as stocks do. Certain types of debt related investment with stocks are particularly risky. If you short a stock, for example, your losses are potentially infinite. And there's nothing really analogous in real estate, if you borrow to buy the chance of a property even going to zero is remote to impossible, right. And the last, in my mind, big advantage of real estate is it's an effective inflation hedge or it has been historically, people think of it like that. And it's true, as long as your taxes and maintenance don't grow by more than one place in your head. And the reason for that is rents are expected to go up at the cost of inflation over time while your mortgage is generally fixed, right. So if you walk in a mortgage for a certain period, and commercial are usually shorter than residential, maybe it's 10, commercial or 30. And residential, it's going to stay at a fixed rate all the while while the rents you collect will grow up. So those are kind of the why and best reasons for me, people will tell you other ones, but those are the big ones. I'm just gonna circle back now because I understand the webinar started a little late. I'm gonna take just a couple minutes to introduce our firm, and then we'll move to the next topics. So Harris Bricken is an international law firm, we do a ton of foreign direct investment, particularly in the real estate space. We have offices in the US here in Portland, Oregon, where I'm speaking and then on your screen, you also have Simone Malinowski. He's in New York City, New York State. And you have Steve Chianglin, who is in our Seattle office, he also works out of Bellevue, which is the nearby office, a suburb of Seattle effectively. We also have offices in places like Los Angeles, Phoenix. And we have international offices in Beijing and Barcelona. So we've been handling this work, I guess, on behalf of inbound buyers, as well as domestic buyers for many years. Steve Simon, and I have probably 40 years of collective experience. And then the greater group, the foreign direct investment group, and the Real Estate Group has a lot more than that at the firm. But that's about it. That's sort of the high level intro I'm sorry for hopping out of order a little bit. I'm gonna turn it next over to Steve to identify urban acquisition

opportunities or talk about identifying urban acquisition opportunities, and maybe Steve could self introduce a little bit better than I introduced him.

Steve Chianglin 8:15

Thank you, Vince. That was a very good summary of the advantages of investing in real estate. And I will be focusing on identifying urban acquisition opportunities. And I would like to add a little bit to been said, one thing that I would like to add is that there is a global trend into a concentration of population in urban centers. And I believe I've read somewhere in the last census that the United States 80% of the US population are considered urban. So although during the short term COVID is dispersing population to more rural areas, the general trend is towards urbanization. And with the general trend of urban concentration, investors should also understand the different urban acquisition opportunities in order to become a better investor. And how to identify urban acquisition opportunities. that's a that's a very big picture type of question. And how I would approach it is that an investor should first focus locally, right? You want to understand the local market conditions, be familiar with the type of projects that you want to acquire? Is it a condo, you know, a smaller project like a single family home, a condominium? Or are you looking into multifamily strip malls retail? Or are you a developer who wants to redevelop a site into you know, let's say vacant land you want to build a great condominium condominium high rise. And so along the same lines, you want to think about the type of market you are that you want to think about the type of market that you want to be in, and also the type of project that you want to acquire. And also the the general market conditions surrounding that investment. So for example, if you are if you want to invest in a gas station, do you want to invest in a gas station when across the street, there's a Costco gas station? Or do you want to invest? If you are apartment developer, you want Are you going to invest in a apartment building, when, in the next several years, there are going to be other apartment complexes going online. So in essence, investing in real estate is like investing in a business, you want to do your homework before putting your money in, and you want to understand and do your research on what other people your competitors are doing. And also, and and do some due diligence prior. Another important aspect of identifying acquisition opportunities is also doing the financial calculations and other pre acquisition due diligence. So some questions I would ask is, does the project pencil out? Meaning does it make financial sense, right? Is your are your if you are buying with that are are your income streams going to be enough to cover the debt. And if you are going to be remodeling or improving a project? What are the estimated costs and the actual costs. And I find that a lot of my clients, they would go into a project with an idea, oh, this is the estimated costs. But when they are actually in the project, the actual costs they find out is a lot higher than the estimated costs. Another thing that an investor would want to consider is prior to enter into a contract to buy a property, there is usually a period of due diligence. And this due diligence period is fairly important for investors so that they can determine the viability of the project. For instance, if if a developer wants to redevelop a commercial site, they probably would want to do a survey, you know, find out what are the underlying you know, if there are easements or any other type of agreements, boundary line issues that would prevent the that would prevent development plants. Or another thing is a very important thing that the clients should consider investors should consider is the environmental issues. So I had a client several years back, they decided to buy a property, they wanted to redevelop into apartment building the building used to house a drycleaners. And so they didn't do they didn't consider too much the environmental impacts of it. But once he bought it, you know, several years past, they thought they were there were they're in the process of development plans, getting their architects, and then suddenly they get a letter from the Department of Ecology saying that, hey, there are remediation issues that you have to remediate. And so with that letter and the subsequent issues that arose, their costs increased over a million dollars. So those are just some of the I guess minefields that a real estate investor would be facing. And you realize that real estate investor will want to consider prior to jumping into the investment. And I think it's very important for the real estate investor to and we will talk about this a little bit later is to get a good group of people that you trust advisors that know the area know the market conditions have gone through the process many times and they will be able to provide good advice before you make the real estate investment.

Vince Sliwoski 14:57

Thanks Steve That's really helpful. You know, one thing we meant to I mentioned at the outset is if people have questions, feel free to type them in, and we'll weave them into the presentation whenever we can best get to them. Next, I'm going to turn to Simon, to talk a little bit about the urban development process. Simon, can you explain that to us?

Simon Malinowski 15:16

Sure, I think what Steve was talking about is a really good transition. And I think it's important at the outset to kind of talk about why we break out the development process. And the way that we think of the development process as a part of separate apart from just real estate investment is it's kind of the out value add component of real estate investment, right. So generally speaking, when a property's being developed, it either involves building from the ground up on a vacant piece of land, demolishing a building that exists already, and then building ground up from the now vacant piece of land, or renovating an existing building. And the reason why people are interested in pursuing those sorts of opportunities is because generally, it provides the opportunity to increase the return that you're getting on your investment, be in the possibility of having a building that you can sell as a whole, or condominium units that are now more valuable that you can sell, or a rental property where you can get more money per unit on a monthly basis. And the reason why it's a little bit of a different process in the urban context than anywhere else, is because generally speaking, and this is a kind of again, generally, but not necessarily the same across various jurisdictions is that developing property in urban areas is a little bit more complicated, a little bit more expensive. There are more regulatory issues to deal with. There are a lot more actors in the sphere, because it's more competitive, and there's more money at stake. And so, you know, the balance in that is, is that generally speaking, when there's more people involved, and it's more competitive, there is a higher rate of return, or at least the possibility for a higher rate of return. But that's kind of what makes the urban development process different than the development process and non urban areas. And the reason why we harp on it is that it is, in urban areas, potentially an incredibly complex and highly regulated process that makes it really important to understand what you're getting into before you begin your investment. And so I thought, what would be really helpful is to just kind of generally walk through what the process is from investment through the end of one development cycle, just to give everyone a sense of what the process looks like. And Steve correctly noted, the due diligence is an incredibly big part of this step one, and that is identifying an actual property to invest in or acquire. And that in and of itself, is not necessarily the easiest thing to do in the world. Because in most urban areas, there's basically a limitless number of investment opportunities and different properties to invest in. And step one is just identifying it. And at that point, you really start beginning to do your due diligence process, looking into what can be done with the property, what the finances look like, where there are opportunities for changing the property. And at that point, you're already beginning to pull in various different advisors, attorneys, architectural consultants, environmental consultants, which Steve pointed out, which can be a huge issue for ground up construction, as you pointed out, because simply missing that small issue could be a million dollar swing in your development budget, you then have to deal with arranging for financing assuming that you're not buying your property for all cash, which almost never happens. From a development perspective. You have to then negotiate and enter into a contract with the seller. Again, ideally, you have various due diligence and due diligence contingencies in the contract. But you already are in the process, then where you're putting down a sizable amount of money for a down payment. You have to compare prepare, construction plans be a renovation or demolition and that ground up construction. You have to contract with someone who actually does the work, which is the contractor, potentially if you won't get into joint venture options, but potentially subcontractors, architects, engineers, then you get to the closing and now you finally actually own the property. And then you actually go through the entire construction process, which involves permits, getting plans approved, making sure that you have insurance, making sure that all of your contracts with your various parties protect you in the right ways. And, inevitably, because it's construction, and it's a complicated, there'll be various disputes that arise over the speed of the project, the cost of the project, people getting hurt on the project. And you know, very quickly, as you start talking about this, you realize what a complicated process it is, and why we talk about it in such a way that in the urban context, it kind of requires a different level of involvement, and guidance, and potentially partnership, because at any step of the process, things can and often do go wrong. And when you talk about, you know, one of the things I mentioned, is obtaining financing as part of the process. And in a vacuum, you know, you can say to yourself, Well, okay, so you've gotten a loan, and you now have this loan, and they helped you pay for either purchasing the property or actually building the property or both. But what a lot of people don't think about initially is that loans have what are kind of part of what are known as carrying costs, which means that even though you have a piece of property that you now own, that is either hopefully, appreciating in value, because you've made a wise investment, until that asset starts generating revenue, either as a rental building or as a building that you sold, you still, unless we've worked out a special arrangement with the bank, and all likelihood have to pay a monthly cost, you have to pay your contractors, you have to pay your vendors. And so any situation in which something goes wrong, because you didn't understand what the process was, or overlooked a potential issue means that you have potentially added months if not years to your development process, during which your bills continue to accrue without actually generating any return on your investment. And so it really does require fundamentally understanding and planning for these issues as you're going through, kind of evaluating the investment and what your options are. And a few things that kind of jump out that are separate from the issues that I've mentioned already, that are really, really specific to urban development, permanent. And I mentioned permanent because every jurisdiction is different. Every jurisdiction is run by its own bureaucracy. They have their own rules about how they want buildings constructed, what the requirements are, how often things are checked, and understanding what that process is how long that process takes. And the ramifications for getting prot steps in that process wrong, are really important. zoning is incredibly important, because if you don't check zoning, if you decide that you're going to do something without fully understanding what the zoning implications are of your property, you can end up in a situation where you start your project. And all of a sudden, it turns out that what you are planning on doing with that property isn't legally permissible. And it happens on occasion, everywhere. It happens surprisingly often in New York, and you then have real issues because you now need to pivot on your project. After making a huge financial commitment and time commitment. New York has a few very interesting, jurisdictional specific issues. There's something known as condo books, which are basically a strange intersection between securitization of real estate and real estate itself, which is you need approval in order to sell condominium units to the market in New York.

And if that's a process that you don't understand, or you aren't familiar with, when you decide that you're going to invest as a foreign investor in a condominium project in New York City, and not starting that process early enough, not understanding the rules and regulations governing that process can be a month if not year long delay. Another really interesting one that we deal with on a really regular basis, our license agreements, which is something that trips up lots of foreign investors, it's something that I'm personally dealing right now with on five separate tracks. Which is in New York City specifically, and this applies in other areas. But sometimes you need access to your neighbor's property in order to build your project safely be found from a foundation perspective, or protecting the neighboring property. And oftentimes that requires getting the neighbors consent. And again, these are the sorts of things where if you don't know that this is an issue, and it's, it can cause all sorts of delays. And this is kind of why and I'm going to kind of pivot to the next topic that we wanted to talk about, which is exploring joint ventures. And partnership is something that we often see our clients do, not just from a foreign investment perspective, but also domestically. And I'll pause for a second to kind of explain what a joint venture is, because it's something that we attorneys throw around on a regular basis. But you know, not everyone understands what it means. A joint venture, the way that we refer to it is basically two parties or more than two parties coming together to get involved in a real estate investment together. And oftentimes, they're referred to either, as general partners are limited partners, and general partners who are more responsible for the actual development process itself, construction, overseeing everything, versus limited partners, who are generally what we refer to as silent investors who are contributing the capital, develop the property. But it is a very common way of basically allocating expertise from the various parties who are coming to a project in the most efficient way. And there are various partners who have different levels of specialization. There's the people who are historically builders, and they oftentimes will come up with less capital as part of the investment. But they actually get into the literally the ground to get the project done, versus the kind of finance investment side who are more responsible for arranging the financing and making sure that all of the books are done properly. And that the numbers all add up at the end of the project. And the reason why joint ventures are particularly useful and important for foreign investment, is because, as is clear, based on I hope was clear that I kind of just went through the issues that are endemic to the urban development process.

If you are coming from a foreign jurisdiction and don't have experience in the jurisdiction, where you're investing, be it New York, Seattle, Portland, LA, anywhere across the country, you don't know what you don't know. And you can get into all sorts of problems by making an investment, because you've overlooked something that you didn't know is an issue. And that can create all kinds of expensive problems, a very kind of straightforward way of shortcutting that issue, and not maybe losing a little bit on the percentage points on what you're making on the project. But increasing the likelihood of success is partnering with someone who is local, who has the market knowledge and the experience with dealing with the issues that are specific to the jurisdiction, and actually helping get from investment to an asset. It's generating revenue for you. And it's why we see lots of people who come in, they facilitate a relationship, they enter into a partnership with someone on an initial project. And if that project goes well, they work on project after project together, because it ends up being a very strong business relationship where people have allocated their resources and their expertise in a really efficient manner. And it just works. Now, there are lots of different ways to go about entering into joint venture, there are different corporate structures, we generally see them as operating agreements, or partnership agreements. And what those documents are, are basically contracts between the two parties that really concretely set forth the terms of the relationship, who is investing what, what their returns are in their investment, when payments need to be made to each party, who's responsible for what Have the project what authority or management is required for every given given step of the process? project? What requires unanimous consent? What happens when things go wrong? All of these sorts of things are issues that we deal with on a daily basis in terms of structuring the partnership agreements in such a way that both sides are protected. And that we kind of account for all of the variables or as many variables as we possibly can for dealing with difficult issues that people aren't expecting that arise, kind of when it when it isn't really expected. And it's, we really have found that joint ventures for a lot of clients is an efficient way of mitigating risk as best as possible when entering into a new market. One of the things I really I was kind of curious to ask both of you about, you know, obviously in New York, we have a lot of, I think, kind of strange real estate specific issues that come up. But I imagine that it is is very similar in Portland or in Seattle.

Vince Sliwoski 31:25

Yeah, I think so. I can answer a little bit for Portland, I think. Yeah, number one, with respect to local zoning code and approving properties and uses and stuff. Like Simon said, every jurisdiction is a snowflake. Everyone is different. Everyone has different zoning codes. Everyone has different regulatory agencies. A lot of times we work with a lawyer or developer or somebody who does this stuff a lot. They will know people inside the agencies here in Portland, it's BDS for the building code stuff. And then there's an environmental agency, and they're where else and there are a lot of overlap there. I say also, one thing that's particular to certain jurisdictions is general market terms, like what stuff sells for right now, right? Like if you were to come to me and say, I want to buy an industrial property in Portland, and it's selling for x, I would run a few simple calculations. And I would say maybe that looks like it's about a six cap a lot of stuff selling at about a six cap right now. That makes sense. You're right now, hater market right now, that kind of a thing. So I think like each jurisdiction is really different in a lot of different ways. I think they're even different sometimes with respective financing, which you think should be more nationalized. And but but it's sometimes not. And especially, you know, you'll find a local bank or a local credit union, that is a lot more willing to be flexible with you, or work with you, if you especially if you have an ongoing relationship. And I found that to be the case with certain clients of ours here in Oregon over the years, and they'll look at things differently to Simone did a good job kind of talking about financing earlier, I want to talk to us a little bit about it, because I think it's so important. I think, big picture. I think, if you're investing in homes, right, and residential real estate, I think those underwriting terms and requirements have tightened up, right. And for good reason. Since the two time 2009 financial crisis, a lot of that was bad underwriting bad loans, people couldn't pay him back, all these mortgages are underwater, it's a little bit different now than it used to be. Whereas commercial underwriting in my experience is a little bit looser. But when you talk about commercial underwriting, you're talking about a lot of things, right? a lender is going to look at a property that needs to be developed a lot different than it's going to look at a property, which is already in use. And when they're looking at a property that's already in use, they're gonna say, Well, what kind of uses it? Is it owner occupied? Are you buying this property to move your business there? In which case we kind of need to look at your business financials and understand if it's under writable in that sense, or are you buying it as a straight up investment property, which I think a lot of you guys on this webinar are thinking about doing? In that case, a lot of underwriters will look at what is the cash flow of the property right now? How much you're going to buy it for? often they'll write to the leases or look at the they'll say, look, this lease looks good as it's got seven years of term left on it. We're willing to give you a seven year note, we're willing to view a 10 year note etc. So I guess I would say that, you know, local issues can be anything from financing all the way down to permitting. And it really, really helps, like Steve said, to do your research, not just on the location, but on the whole local environment. That would be my sort of high level meandering answer to someones question. I don't know if Steve has input.

Steve Chianglin 34:41

Yeah, I think on top of that with with respect to jurisdictional issues. So I mostly my offices in Bellevue and across the across the freeway across the water there in Seattle. The city council has recently proposed A lot of very tenant favorable statutes that prevent landlords from exercising their rights under the lease agreements. So, so in order to, to, for inventory, the key thing, I think what Simone and Vince has been talking about is that he is having enough cash flow to generate value for the property and to cover your expenses, and you can get their appreciation when you exit the property. But during the project, if there are municipal codes or city codes that are being created or promulgated by, by, by, I guess the, by the people in charge that are not favorable to, to the landlords, then, you know, that is something unexpected. And that's kind of what is going on in Seattle right now at this point. And of course, I understand that during the pandemic, there is a big push to protect tenant rights, so that they can get over this period where a lot of people are not are away from are not able to work and earn income. But at the same time for landlords, some of these smaller type of landlords, are they still have to make their mortgage payments to cover their lender obligations? And if they don't cover it, then you know, the lenders have ability to foreclose on the properties. So to answer someones question, I guess to address this issue is that there are different jurisdictions even in Seattle and Bellevue, just 15 minutes drive, the landscape, and the laws are very different.

Vince Sliwoski 36:59

Yeah, I think that's a good summary. And then the laws can change pretty fast, right? Like with the stuff Steve was just talking about, we had eviction moratoria here in Oregon, on both the commercial and the residential side, but they were they were different, right. And they're ending differently. And even when they end things will be different, right? Like in Portland, it's, it's hard to be a landlord. And people complain about being a landlord, you've got a little local registration thing. And attacks if you're a residential landlord, and if you want to get your client, or if you even if your clients lease is up, and you don't want them to say you have to pay for them to move, right. That's pretty radical. No other jurisdiction has had that that I know of in New York has things like rent control, Portland has some version of rent control. I don't know on your trend control works, if that really matters for investors small talk more about that. But I guess just getting back to this point of like, really understand where in what you're buying, understand the laws understand what laws may be changing, and what's on the horizon and what the general sort of tenor of the environment is before, before diving in.

Simon Malinowski 38:01

I think that's a fantastic point. And, Steve, you mentioned that as well, which is kind of the rent issue. The jurisdictional specific issue, like rules related to that, really dramatically change the long term value of an investment, and is one of the things that are really looked at Ben's, to your point when banks are evaluating whether or not to make a loan on an investment. I mean, to your point in New York, it right now takes a year to invest evict a non paying 10 to COVID aside, and it is an incredibly tenant friendly jurisdiction. And they've changed the rent stabilization and rent control laws, very recently that severely decreased the value of multifamily property in New York City. And the reason for that is, is that you basically have lost a lot of the opportunity from an investment perspective, to increase the revenue generated by your property. And you have the potential for losing months, if not years and brand based on the landlord tenant laws. And so I actually think it's a really good segue in terms of talking about assembling local advisors. But these are the sorts of things that, again, are issues that you just don't know, unless you either are very diligent resource at researching it, or have advisors who kind of tell you about what these issues are as part of evaluating the investment opportunity.

Vince Sliwoski 39:46

I think it's good. We pivot and talk about that. I just want to answer a question that came up because I don't know when we're going to get to it out of order. Somebody asked, you mentioned the stepped up basis on death of an owner. Are you concerned that the current political climate might remove that advantage? Yeah, okay, so yes, short answer is yes, the Biden tax plan, whether it'll get done or what will get negotiated and hammered out, when nobody knows, obviously, but the way it kind of works is currently when you pass away, and you leave something to your heirs in this case, say a house residential property, they inherit the property with a basis of whatever the fair market value was on the day that you died and pass it to them. Right. I mentioned that earlier. So what Biden's talking about is he's talking about taking away that step up in basis, basically, your heirs would inherit the property at whatever your basis was. So essentially, people would people would characterize that as a tax on death, is it? Is it going to happen? I don't know. It seems like you right now, they're talking a lot more about infrastructure. I don't know if the tax code will change. I don't know if I'm, I would accurately say I'm concerned that the current political climate might remove that advantage. But it's an advantage that people often point to as an unfair advantage for real estate investors under the tax code, and I would take advantage of it. While it's here. Appreciate it while it's here, who knows what's going to happen? Alright, so that's my two cents on that. But let's talk a little bit about assembling local knowledge or local knowledgeable advisors. I think Steve was going to lead on that.

Steve Chianglin 41:22

Sure, sure, yeah. So having local advisors or I think it's a it's a very important to have good local advisor, because the urban development process could be very complicated and requires different groups of people who specialize in certain things, to be able to provide the investor with good advice. And, and one key local advisor that I think all investors should have is to have their good trusted real estate agent or a group of real estate, realtors, who know the lay of the land intimately. They know the market conditions. And they are out there, because they're talking with so many different groups of buyers and sellers, they interact with different, you know, architects, attorneys, they are the ones that if you develop a good relationship with they are the ones that are prospecting for you. And when you have a lot of these real estate agency are working off of a commission structure, meaning that they will try to bring you deals and if it is actually a deal that closes then they get a commission, usually from the seller. And, and so these these people, these agents are very important in helping the investor understand the lay of the land, and they in essence help you. They give you the advice on being able to gain profits on your investment. Another group of knowledgeable local advisors, when After identifying a property, and while you're doing your due diligence is getting a group of architects, designers, then use professionals, engineers, there is the they are the ones that assists you to help you realize your plans. These advisors, professionals understand what are needed during the permitting process. They help you build and design your buildings redevelopment process, and they are the Knowledgeable professionals that understand the local jurisdictional issues, right? For instance, Seattle, and again, Seattle and Bellevue. Development codes are different. So having these professionals on your side, they will be able to tell you, hey, you had this in Seattle, you have to watch out for this. But if you're in a different city, you want to be able to look out for a different issue. Another group of professionals that you will be dealing with are the general contractors and contract subcontractors are the ones that do the actual improvement or the value added of to the property. And they are very important because they help you understand the costs, the estimated costs of your projects. And since they're the ones that you will be hiring to build out your plans, they will also give you some ideas of a the possibility of an additional cost that you might not be anticipating and another group of professionals that all investors should should be working with our attorneys. And so as an attorney, I I it's A little bit self serving here. But we seen a lot of different contracts. And we dealt with many different types of clients, seeing them through the entire development process. And we understand the pitfalls, the mind, the minefields that, you know, clients in the past have. Father attorney allows you to understand your downside risk. And hopefully, a good attorney will be able to advise you on certain ways to minimize those things. And a lot of these local advisors Lastly, I think a lot of these local advisors is that it's a, you want to develop these relationships over time, like Simone said, you know, these, you might get lucky. And the first time you work with your joint venture partners, or your, your local advisors, you find out, hey, they are great, they're very good at what they do. But a lot of times, you'll find out these advisors will require some time to develop, as you get to know them. And as they understand your, as they understand your investment purposes.

Vince Sliwoski 46:22

That's great. I think it might be a good time to talk a little bit more about navigating urban construction issues, Simon, Are you interested in leading on that?

Simon Malinowski 46:30

Yeah. And I think that that's kind of, Steve, what you just finished on is a perfect starting point for that. Because, you know, the way that every contract, or every development process starts, as always, with the best intentions, and everyone is always very excited at the closing, because they now have a brand new shiny asset, where they're, you know, just looking at the returns on their investment at the end. And what lots of people don't think about is what happens between the closing and when you actually are generating revenue from this asset that you've purchased. And in the development context, and that requires going through the construction process. And the reality is, is that for, for almost everyone, and it's an opaque process, it's one that you don't really know until you get involved with it on a project basis, and you go through it the first time, and then, you know, more times after that. And, you know, a great example of this is, uh, you know, I from personal experience, I, you know, I've negotiated hundreds of construction contracts with contractors, and I talked to both of you about it, but we're, you know, renovating our house for the first time. And it's this is the first time that I've actually been on a construction project on a day to day basis. And you begin to realize that there are certain parts of every project that are a little bit different, and without having full understanding of what the cost is on a daily basis, and all of that, it makes it it makes the process just a little bit harder. And so the way that we help our clients navigate construction issues, throughout the process, is step one is always always always betting the contractor that you're getting involved with. And there are lots of different ways of doing it, there's the direct way of doing it, which is getting as many referrals and finding out what the contractors experiences and seeing whether or not there are violations issued against them in the local administration or whether or not you you know, your broker has had experience dealing with this contractor and having all sorts of issues. Another important part of that, and this is I'm still talking about betting the contractor is, is through your architect, and if you find an architect that you're comfortable with, and that you decide to work with, in a lot of ways the architect becomes the owners, eyes and ears on a project.

And oftentimes, an architect's agreement is the has an owner's rep component to it. And what an owner's rep is, is literally that the owner's representative on the project. And they're the ones who are really not only responsible for preparing the plans pursuant to which work is going to get done. But actually going to the site on a regular basis, and making sure that the work that's going on as part of your development is actually what it's supposed to be that foundation is being poured correctly, that if you're doing some sort of waterproofing work that the waterproofing materials are being done properly, and that basically things are going in the correct order and being done the correct way. And, you know, once you've identified the contractor that you're, you know, you've decided that you're going to go forward with the actual construction contract is oftentimes the most important document with respect to the development process, because it is critical to one, both preserving your rights as an owner in terms of issues that may arise during the process, which often do happen, but also when drafted correctly, and creates a very powerful and important disincentive to the contractor for bad actions are taking too long in the process for not doing work properly. And there are lots of different ways that that should be accounted for the biggest areas that we see that that that I think are almost most important when kind of preparing for construction issues is our delays. Because again, as we talked about before, where there are delays in the project, it has a real day to day value in terms of carrying costs on an investment, and contracting properly for what happens if there are delays, and who are responsible with those associated costs are really important. How disputes get resolved with the contractor in the event of again, delays or defective construction, when there are issues that come up. And then the last one, which which happens with unfortunate regularity, and but it's a real part of the construction process. across the United States are injuries, workplace injuries that take place on the development side. And the reason why that's so important is that without having the proper insurance without having the proper defense and indemnification language in a construction contract, as the property owner, in many jurisdictions, you're at risk to be liable for someone who gets hurt either walking by the project, or working on a project to the tune of potentially millions of dollars in worst case scenarios, which very easily could be the difference between having a successful project and having a project that's lost money. And so it's really important to make sure that when you are at the onset of construction, that you have a contract that really protects your rights, but also that accounts for all of the issues that may come up. And you know, it, I cannot stress and I know that this sat may sound a little bit self serving, but I cannot stress the importance of having an attorney who understands the construction process, because if small things are overlooked, it creates the potential for being in years, years, literally years long litigation over issues that arise and few other major things that come up as part of construction issues in the project. mechanic's liens and payments, which is in the event that there are issues over work that's been done and whether or not the contractor needs to get paid. in many jurisdictions, the contractor has the right to buy the lien against the property, which can make it very difficult, if not impossible to sell, to refinance, potentially has the impact of foreclosing your ownership in very rare circumstances.

But it's really important to understand those issues and to protect against them as you're going through the process. Because if you don't it again, can really have an impact on whether or not the project is financially successful or not. And the last, the last thing that I promote urban construction issue perspective, all of the I think this really does apply across the board is issues that you discover after the project has been completed. And that really very often happens because lots of underlying construction issues kind of don't get revealed until a year two years three and three years after the fact because, for example, water infiltration is not something that happens the first time it rains, but the 100th time it rains, if your building hasn't been constructed properly and there isn't the proper water and below to the building. All of a sudden if You're a rental building owner, you have leaks in your building, and you have tenants who are refusing to pay because every time it rains in Seattle, water is dripping down the sides of your tenants walls. And, you know, understanding kind of boats making sure that the work is getting done properly during the course of the project, but also having the right protections in place for issues that are discovered after the project. And every state has its own statute of limitations and various warranties that are automatically in place with respect to new construction. And these are all things that are really important to be both aware of, and to plan for, as part of actually undertaking an investment in urban real estate in the US.

Vince Sliwoski 55:56

That's great. I think just because we had a little bit of a late start, we could go just a few more minutes. And I'd like to take the opportunity to talk about contracts and answer a particular contract question. Looks like somebody wrote, do you all like AIA? contracts in general? Are there particular clauses that repeatedly cause trouble in this arena? How do you resolve generally, I have a few thoughts about AIA contracts and contracts in general. But I want to kind of defer and see if Steve or Simon have particular thoughts before.

Simon Malinowski 56:26

I as simply as possible. I think that AIA contracts are a great starting point. And beyond that, they all require real customization to really make sure that you're protected, and that you understand what the issues are. And that's kind of the beauty of the AIA that they've created very good baseline that is customizable in a way that that can work. But I think that it is. I like them. I my standard form is generally not an AIA, although, you know, I've had clients who prefer working with them to the second part of the question I think I saw, which is clauses that repeatedly cause trouble. This, in many ways, the single most important provision in any contract with the contractor is dispute resolution. And there's a lot of different ways that that provision can be structured. Oftentimes, there is an initial decision maker, where the architect or another third party is designated as the person who's supposed to resolve those issues. And it's a very cost effective way of dealing with issues without resorting to litigation or arbitration, which immediately becomes very expensive for all parties, and how much pushback you get on how that provision is drafted, when dealing with the contractor really kind of gives you a pretty good indication of what you're going to be dealing with over the course of the project.

Vince Sliwoski 58:06

Thanks, Simon. Steve, any any thoughts on AI contracts or contracts? in particular?

Steve Chianglin 58:12

Yeah, I think the it's very important for the client to understand the documents, whether it's AI or anything that's customized. And also, to add to that is just understand your needs. And you want to communicate that to to your advisors. Because even though there is a baseline, and while you're negotiating, if you don't understand what your needs are or or your desired outcome, a lot of these these contracts could come back to to haunt you in the future. So all I can say is understood AIA's are great. But understand what's in them.

Vince Sliwoski 58:59

Yeah, I think I agree. I mean, to the extent we have an industry standard, AI is the standard, you see them a lot. I like that they're customizable. I like them more, if I'm representing say an architect and a subcontractor for various reasons. They limit subcontractors access to information in a lot of cases, they give the architects a lot of power. They're good agreements. But I mean, you can't just use an agreement you off the shelf agreement in general. That's the general thing throughout the law. And I think that's true with construction or property acquisition contracts, whichever it is, I think you've got to look closely understand we're getting into understand that a lot of things are highly negotiable. Markets are different, something that may be market in one place is not marked in another place, whether that's period you can do diligence, whether that's which contingencies you can ran into a contract, whatever. I think you just have to work with people who can navigate those contracts, but I think they're good forms to start with. That's how I would think about them. Okay, guys, we're at almost 12:05 I think we started few minutes late, but we want to be respectful, very It's time to log off. We'll replay the webinar at some point on one of our law firm blogs. There's a Harris Bricken blog you can find. Thank you very much for joining us. Thanks for your questions. We appreciate everybody's input and we'll see y'all soon.

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