

TALES FROM THE TRENCHES™

By Barry C. McGuire

“A Deal That Went Bad and the Lessons Learned”

This edition of the *Tales from the Trenches* podcast features special guest Arden Dalik, a senior advisor in the Calgary office of Global Governance Advisors. Her Tale concerns a real estate investment project in Alberta presented to the REIN Group by a REIN member. Quite a number of REIN members invested in the project, including Arden. Unfortunately, the deal went bad, but I was able to come to Arden’s rescue as her real estate lawyer (aka Legal Eagle).

As always our purpose in *Tales from the Trenches* is to educate and be educated, getting better at real estate investing by learning from experience. This Tale is not a “poor me” story all. It is all about education, sharing, and, as Don Campbell so often tells us, “being in that tiny percentage of people who face adversity and push through it rather than run from it!”

At the time that this Tale started, Arden had been a REIN member for about 1 year. She owned 4 revenue properties, having purchased using realtors, from FSBO’s (For Sale by Owners), and through other REIN members. Arden also had a couple of joint venture partners. She was definitely a little beyond the rookie stage at that point—but still not an expert.

What Was the Real Estate Deal?

Purchase condominiums in an emerging area of Calgary.

What Was Required to Invest?

\$10,000 down per unit.

Sellers Marketing Ideas:

Presented as a potential group project to renovate, market, and flip.

How Was the Deal Structured?

A large number of units were purchased wholesale by the vendor. A wholesale purchase is when someone buys a number of units at the same time in order to get quantity discount (i.e. they pay less than full market value). It’s kind of like the Costco concept for real estate!

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Anyway... as part of the wholesale purchase agreement, the purchaser cleverly negotiated a financing plan that would make the properties more attractive to the investors. They all had assumable mortgages on them. He then negotiated a second mortgage as a vendor take-back in order to minimize the front-end cash closing costs required for investors to participate. This vendor take-back was for 6 months, which was designed to allow the investors time to renovate, market, and sell the property before they had to pay out the second mortgage.

How Did Arden Approach It?

With a joint venture partner financing it 100% as an investment.

What Went Wrong and How Could It Have Been Prevented?

Below, our Keen Investor (Arden) explains how the deal went, and the Legal Eagle (Barry) comments on what they did—or could have been done—to avoid all the trouble.

KEEN INVESTOR (Arden Dalik)	LEGAL EAGLE (Barry McGuire)
Hi, I'm a keen investor and this is my story. I had been trying to get to work with a group of REIN members especially this one TOP REIN member because he seemed to have the MIDAS touch (and I wanted some of it!). Finally I got my chance. I got ...THE CALL. BUT... I had to buy right away because they said others were "waiting in the wings" if I didn't grab it now it would be gone.	Don't feel pressure to buy. Always do your due diligence.
I didn't review the condo docs because a Reserve Fund Study might as well be written in ancient runes for all I knew about them! But I was buying from a top REIN member and he had looked at the study. So I didn't have to worry about it because he had reviewed them and told me they looked fine! And a bunch of other very experienced REIN members had already bought in so it must be fine!	If you don't know how to read a Reserve Fund Study, then get your real estate lawyer to help you. Don't take someone else's word for it!
I called my investor and had him make the deposit cheque out for \$10,000 to the seller's company.	Always send cheques in-trust to the lawyers, who will make sure that the money isn't released until the deal is done properly.

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KEEN INVESTOR (Arden Dalik)	LEGAL EAGLE (Barry McGuire)
<p>I was told that we'd both use the same lawyer – it'd be easier because we were doing a simultaneous closing. The lawyer would be in touch with me for the closing. Now we just had to wait for 5 months for our possession date.</p>	<p>Always get your own legal representation because you need someone looking out for you and who doesn't have a conflict of interest. This will become painfully obvious soon...</p>
<p>While our possession date was a long time coming, many other investors were immediate. Hence, there was a flurry of activity related to renos in the first couple of months, which my investor and I got quite involved in since it would be educational once we began our own process. There was a lot of excitement and energy early on. Similarly, there was a joint marketing effort with open houses, shared costs for flyers, etc. in which we keenly participated. However, things were not going as planned. Everyone was having trouble selling their units. As a result we were around to watch the initial excitement of other investors who were already marketing their properties diminish to disappointment and in some cases frustration and anger. Needless to say it was a little tough to keep my investor “motivated” about our pending closing when we were surrounded with units that were not selling. We started looking to a Plan “B” – i.e. Buy and Hold – rather than Fix and Flip... before we even got the property. Essentially, the feedback was that they were beautiful inside but people couldn't get “past” the outside of the condow complex, which was a disaster. The windows were rotting and falling out of their frames. Some doors let snow blow right into the homes in the winter. Garbage bins were falling apart, fences were badly broken, and the stucco was crumbling off the structure.</p>	<p>You must be prepared to consider alternative exit strategies for your investment properties. You might be able to just walk away. But once you've got an unconditional purchase contract, you will lose your deposit—and possible more (see this related blog post and podcast). In that case, Buy and Hold might have been a good choice when Fix and Flip didn't work out.</p>
<p>A number of investors, including myself, decided to get onto the Condo Board to clean the place up. I also wanted to learn about Reserve Fund Studies for the next time I purchased a condo.</p> <p>It didn't quite turn out the way we planned. (None of the Board Members have so far been nominated for the Miss Congeniality Award!!)... This was, as Oprah would call it, one of those Ah-Ha Moments! We have all learned an</p>	<p>This is how to turn a negative experience into a valuable one: try to learn something from it.</p>

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KEEN INVESTOR (Arden Dalik)	LEGAL EAGLE (Barry McGuire)
<p>incredible amount about Condominium Corporations, which will help our present and future investments including:</p> <ul style="list-style-type: none">⇒ Reading and understanding Reserve Fund Studies,⇒ Understanding Condo Bylaws including pet and rental restrictions,⇒ Balancing the needs of all owners in a complex,⇒ Assessing the potential issues with the surrounding area, not just the immediate complex,⇒ The cost of desired improvements to a large structure, and⇒ Structuring special assessments. <p>The group of investors was incredible about sharing with each other. (Even with the “unpopular” Board Members). So in addition to learning about condos, out of creative necessity we also learned about:</p> <ul style="list-style-type: none">⇒ Selling with wraps,⇒ Structuring Lease Options,⇒ Qualifying the condominium for CMHC financing, and⇒ RRSP mortgages.	
<p>About one month before closing I decided to call the lawyer and see what was coming up. What did we need to do, I asked, so that I could inform my investor. I never got a call back. Then two weeks before closing I called again, I never got a call back. My investor began to ask questions that I couldn’t answer... it was embarrassing. Closing came and went; no returned calls.</p> <p>Then I called the seller and he tried to get a hold of the lawyer. He got back to me right away and said that there had been a problem in the lawyer’s family so he was “falling behind with his cases.”</p> <p>6 weeks after many unreturned phone calls to the lawyer and some returned calls but unfulfilled promises, I finally had a “duh moment” and realized that I needed my own independent legal advice.</p>	<p style="text-align: center;">See, I told you!!!</p>

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<p>I called in my trusty legal advisor, whom I had used many times before, and explained the situation. Essentially it shifted from me getting ignored by the lawyer for free to me paying my own lawyer to get ignored by the seller's lawyer! (Ok, ok it was a bit more than that!) I'll let Barry finish the story...</p>	<p>The lawyer lost his license to practice law in Alberta, and they never did close on the condominium. Luckily, my law firm, RMLO Law LLP, was able to get the investor his deposit money back from the seller 9... months from the initial date of deposit. It could have been much worse without getting the deposit back from the seller. We actually had litigators ready just in case we had trouble getting the deposit back because it hadn't been made out to a lawyer in-trust...</p>

Lessons Learned:

Real Estate is what happens while you're making other plans! If you do your due diligence properly, then you can avoid a lot of problems before they become serious. But you should still be ready for Plans B and C; they may just turn out to be even more profitable than your original plan. Don't panic, use your creativity, and call your real estate lawyer!

**FOR ALL YOUR ALBERTA REAL ESTATE LEGAL NEEDS,
CONTACT BARRY MCGUIRE TODAY!
EMAIL B.MCGUIRE@RMLO.COM**

**RMLO Law LLP
Suite 101, 10301-109 ST Edmonton, AB T5J 1N4
Phone: [780.431.1444](tel:780.431.1444) Fax: [780.431.1499](tel:780.431.1499)**