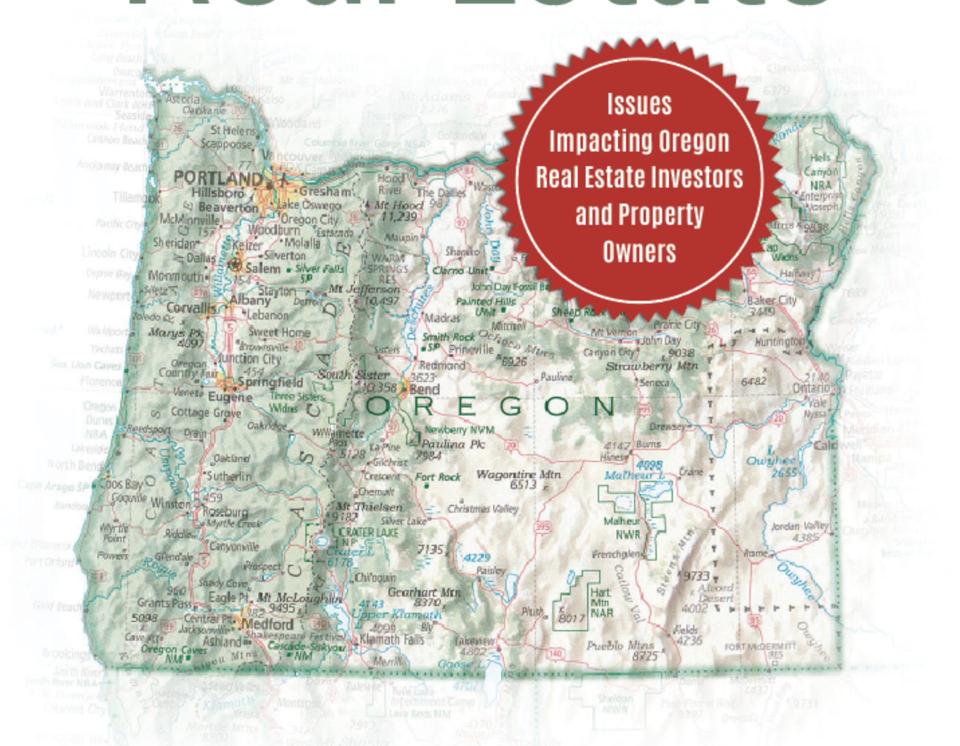
Disruptions In Oregon Real Estate



Issues Impacting Oregon Real Estate Investors and Property Owners

René Nelson, CCIM, CRE

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Here's What's Inside…

Introduction

Following a statewide rent cap, Oregon multifamily investments dropped thirty-eight percent (38%), according to a recent article from the Costar Group. I hear from Oregon real estate investors that their biggest issue is confusion surrounding new rent control laws and how these laws may adversely impact the value of their properties in Oregon. Where can they find the most up-to-date information they can truly trust? Many are wondering about their options, given their current situation. That led me to offer a service called a commercial property analysis.

My commercial property analysis report shows you, the investor, the amount of equity held in your properties; also, it provides you with strategies on ways to use your property to create more positive cash flow as well as showing you ways to meet your income goals. I also work with clients to educate them on available options. For instance, they want to do a 1031 exchange that will move them out of their multifamily properties and into a new property class, or into a new location that could put them into a better financial situation. This is certainly possible.

I know you're busy and it's hard to keep track of all the changes occurring in the state of Oregon as well as across the nation. Many of my clients find their decision-making bandwidth is taxed by all of their responsibilities, not to mention that tracking changes has become a full-time job, from tracking new state regulations for multifamily properties to tracking national changes from government impacts like the new tax code. I offer experienced guidance and counsel to ensure the proper information has been made available, so you can make the appropriate decisions.

My true passion lies in helping Oregon real estate investors analyze and measure the value of their current real estate portfolio while exploring the available opportunities. I also want to be a resource for my clients. Despite significant market disruptions occurring in the economy, I have helped my clients understand the impact of events in the state and national real estate markets, and how it can affect their property values. Also, we explore ways to grow their portfolio during this disruption and show them how to continue to be savvy investors.

Working with my investors over the years, I've found an educated client makes better investment decisions and, in the long run, feels much happier with those investments. Predicting market cycles seems impossible. Investors often struggle to identify trends in the U.S. economy and the capital markets but end up waiting until it's too late. It's easy to get caught up in the analysis process and end up missing the window to act on opportunities that could have created a positive investment decision.

My desire for you, after you've read this book, is for you to continue becoming an informed real estate investor on issues impacting the state of Oregon as well as the national and international markets. May you make better-informed decisions with the latest information available.

Sincerely protecting your investment properties,

Rene'

Counselor of Real Estate and Real Estate Broker

Chapter One: Owning Commercial Real Estate Investments in a Volatile Environment

The recent state regulations have added a new layer of uncertainty for Oregon real estate apartment investors. My apartment clients have responded with a range of reactions. Decisions you make in the future will affect your bottom line, the amount of cash flow you will receive, and your comfort level with your investment portfolio. For those of you who have concerns about the shifts in tenant rights due to the new Oregon state rent control laws, I can tell you it will only continue to get tougher in the next several years.

As an investor in the Oregon real estate apartment market, until quite recently I felt very comfortable with my investments. As long as there was a net migration of people into Oregon, I could fairly accurately forecast my property's level of acceptance and anticipated net operating income because it was a stable market. But now the state has the right to tell me at what level I can increase rents, and that I will only be allowed to increase it annually. They have also removed my ability to give a No-Cause Notice to get rid of an unruly tenant.

A New Minimum Low

This has made it more difficult to eliminate a disruptive tenant to protect the living environment for the rest of my good tenants. When new laws pass in Portland for multifamily they typically then pass statewide. We saw this when rent control passed statewide. Recently, the City Council of Portland introduced new ordinances addressing how landlords screen their prospective tenants. The Fair Access in Renting ordinance, or FAIR, will create a first-come-first-served system for rental applications, prioritize accessible units for people with disabilities, cap the income-to-rent ratio that landlords can require of their tenants, and place some limits on the use of credit and criminal histories as a criteria for denying a person’s rental application. One of the controversial measures will prevent landlords from refusing to rent to someone with a credit score as low as 500. The ordinance is set to take effect on March 1, 2020. The ordinance's "low-barrier screening process" offers to landlords a standard set of criteria, which allows rental candidates who have gone at least three years without a misdemeanor and seven years without a felony to be considered. "Perhaps the most troubling in this policy is the lack of exceptions for people convicted of violent crimes, even rape and murder, in the low-barrier screening process," said Portland Commissioner Amanda Fritz who voted against it. Some key points in the "Fair Access in Renting" Ordinance: **First Come, First Served:** Landlords must use a first-come-first-served application system for units that are available for rent. They are required to give 72 hours' notice before they begin accepting applications for a unit. People with disabilities get priority for accessible units. **Identification for Applicants:** Applicants do not have to provide proof of citizenship for government-issued photo ID if they have other forms of photo ID that can be reasonably used to verify their identity. **Income-to-Rent Ratios:** Landlords can require applicants to have income that is 2.5 times the rent for less expensive units with monthly rents affordable (as determined by HUD) to making at or below 80 percent of Portland area's median family income.

For more expensive units, with monthly rents above the affordability standard, landlords can require applicants to have income at most 2 times the rent. **Criminal Background Checks:** Landlords are encouraged to use a standard set of screening criteria. According to those criteria, applicants sentenced for a felony conviction more than seven years prior or sentenced for a misdemeanor more than three years prior would not be denied. Participation in a diversion program, expunged convictions, and juvenile justice system proceedings would also not be reasons for denial. Landlords could apply more stringent screening criteria, but if they do, they must give applicants an individual assessment and the opportunity to file an appeal. **Credit History Checks:** Landlords could not reject an applicant with a credit score of 500 or higher. **Screening for Other Adults Living in a Unit:** Only the applicant can be screened for their financial history. Other adults who will be living in the unit cannot be screened for their factors related to health, safety, and property maintenance (e.g., a person's criminal background).

The new ordinances will not reduce rental costs and, in fact, will most likely add new costs for tenants because landlords will be forced to administer new rules regarding tenant deposit and screening deposits. They also just passed a $60 a door tax on all multifamily properties in Portland. This fee will cost the typical 60-unit apartment building $3,600 per year. Funds generated from this tax will be used to fund a new enforcement division to enforce fair-housing laws, mediate landlord-tenant disputes, and ensure that landlords are meeting the new requirements,. According to Deborah Imse of Multifamily NW, the new policies will lead to more housing instability and, ultimately, more homelessness. All of these recent state changes could have a serious impact on your bottom line and the amount of cash flow you can receive from your multifamily property.

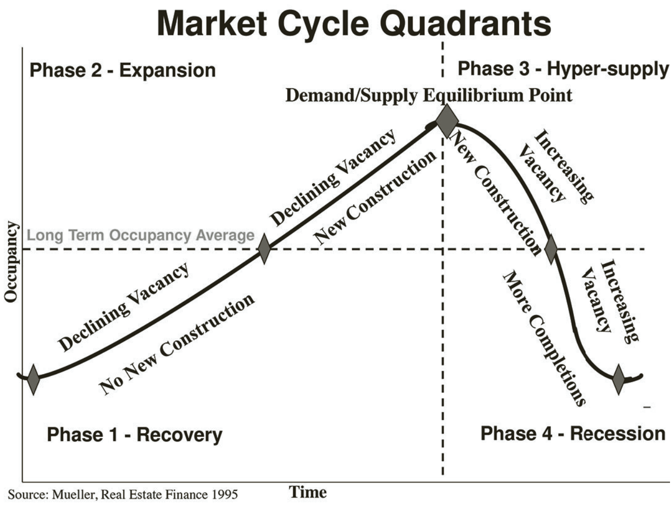
Some investors are taking a wait-and-see approach because they are unsure of their options. Some national market disruptors are indicating our economy could be changing and that our current phase of the real estate cycle is about to shift. Perceived market volatility is in the eye of the beholder.

The more you understand the variables and influences as well as the appeal and the value of your investments, the less prone you will be to make poor decisions that could cost you money. Ultimately, understanding the multifamily market and related events will make you a savvier investor. At some point you may decide that you want to sell and transition out of multifamily. Death, debt, and divorce as well as myriad other factors typically force people to make changes with their real estate portfolios. I often deal with investors who want to consider their options of either doing a 1031 tax deferred exchange from multifamily into a new type of commercial real estate like a triple net (NNN) leased commercial property or who want to consider selling and paying the capital gains tax and moving their money out of multifamily. Understanding the objective measurements used by an investor for buying property is important. Becoming an expert on those measurement systems takes years to refine, but I have spent my career doing that and can show you how to understand the variables that influence those measurements.

There are four phases to a real estate cycle.

The *first phase is recovery*, and the *second phase is expansion*. In this phase, developers start to add more units into the market, and lenders become more lucrative in their lending opportunities. That typically creates a peak in new construction. That's where the demand and supply equilibrium point hit that sweet spot. Shortly after that, the market heads into the *third phase of hyper supply*, where increasing vacancy situations appear and increased completion of new units coming into the market. Unfortunately, then the market often rolls into a *recession, or phase four*.

As we all know, a recession is a part of a normal business cycle; it's difficult to predict when the next one will start and how long it will last. Knowing what you are doing is important because it will allow you to take advantage of market opportunities.



According to the *Multifamily Northwest Spring Apartment Report* of 2019, the Portland apartment market is entering the late stages of the hyper-supply cycle. In Oregon, the homeownership rates are increasing primarily because interest rates are still low, and the population growth is starting to slow.

Vacancy rates are starting to increase while rent growth is slowing, and apartment construction in the Portland area has slowed. Indications show the Portland market will soon be reassessed; over the past five recessions, Portland has been a leading indicator of the health of the apartment market in the balance of western Oregon.

Currently, there are over 10,000 apartment units under construction in Portland with a projected absorption rate of 5,000 to 6,000 this year, causing an oversupply of new units. Unfortunately, market stagnation weakens the appeal to out-of-state investors. We're also seeing increased vacancy rates, which will become a much more measurable factor in altering the investment real estate market appeal.

Vacancy Rate Increase

Over the past several years, vacancy has not been an issue. It has been in the 1–3 percent range. If a vacant unit existed, it would simply be rented. A recent Multifamily Northwest Rent Survey of more than 63,000 units from 900 properties showed vacancy had increased in the spring of 2019 more than half of a percent from the fall of 2018. Now a vacancy rate of nearly 5 percent has appeared.

Unfortunately, a natural reaction for increased vacancies is that incentives must go up. As the rental market softens, owners will have to offer rent incentives to attract quality tenants. The survey found that over 9 percent of properties in Portland were already offering rent incentives. A similar survey of the University of Oregon housing found a 22 percent vacancy factor (even with incentives) in the campus area, proving an oversupply of apartments in the Eugene campus area.

Incentive Examples

Right now, some property managers are offering $100 off on your first-month rent. I have also seen managers offer a free iPad for a one-year lease, and when the market shows a larger slow down, managers will typically offer an entire month of free rent. If you sign a 12-month contract, they'll give you the 12th month free. Managers haven't yet reached that point in our local market, but those have been some of the measurements I have seen used in the past.

Increasing vacancies will affect your bottom line by reducing your net operating income. Couple that with fewer out-of-state investors interested in Oregon multifamily properties and it could be a recipe for troubled times. According to Multifamily Northwest, "Changes in recent rent control is an increasing concern to both in-state and out-of-state investors." The investor market is reacting adversely to the statewide rent regulations. Knowing your options now and getting ahead of the market is a wise idea

The new regulations can significantly and adversely impact both your property value as well as future buyer appeal. For those of you who have chosen to own apartment properties, you need to become an expert in owning and managing apartments under the new market changes. The more the state becomes involved, the less the investors will like it. I want to speak to that portion of the market who finds commercial apartment investing to be their cup of tea. Other upcoming topics will be rent control and the new laws that factor in for tenants.

Oversupply Becoming a Problem

Regarding oversupply, the problem is not just happening in Oregon. For example, I recently spoke to a broker in the Reno-Sparks market, who indicated there were 15 subdivisions of newly built homes in the $450,000 to $500,000 price range. Each of these subdivisions has approximately 90 homes; the same developer built all 15 of these subdivisions. Now the market has changed, and they are experiencing a lack of demand, which in turn has the subdivisions competing against each other, trying to sell off properties.

Often what we see in a hyper-supply market is there is more new construction compared to the past. Interest rates begin to rise. Rent growth starts to reach a slower pace; while it's still positive, it tends to slow. Some property owners start to experience rent concessions as the new properties appear on the market. Apartments become increasingly difficult to lease, or in single-family residence situations, increasingly difficult to sell.

In my experience, the investor's mood turns from happiness ("Getting this to the market is great") to more of a cautionary mood; sometimes they even go into denial and believe that there's not a problem brewing. Some investors are confident it's just a bump in the road and the situation will self-correct as long as they don't panic; but if they don't pay attention to what's happening, they could be caught in a recession. That's what happened to a lot of builders in the last recession. Many builders were caught with an oversupply of inventory in the market and couldn't sell their properties. Unfortunately, a lot of builders went bankrupt, both apartment developers as well as single-family developers. Know your options and what your next move is.

Chapter Two: New Laws Favor Tenants in Oregon

On February 28, 2019, Oregon became the first state in the nation to pass statewide rent control. Senate Bill 608 states: The landlord cannot raise rents in the first year of tenancy. It also limits future rent increases in 12 months to 7 percent plus the consumer price index, as published by the Bureau of Labor Statistics in September of the prior calendar year. Currently, the rent control cap in the state of Oregon is 10.3 percent. The cap on increases applies to all new renewals and to all rent increase notices that have been delivered on or after the February 28th date.

If a landlord terminates the tenancy of a prior tenant with a notice of termination but without cause during the first year of occupancy, the landlord may not increase rent for that unit by more than 7 percent plus CPI when the subsequent tenant moves in. If the landlord violates the rule, either through wrongful termination of a lease or a rent hike higher than 10.3 percent, the penalty for the landlord is three months of rent plus damages (i.e., a tenant's attorney fees).

Rent control also applies to manufactured homes as well as dwellings. Senate Bill 608 greatly changed a landlord's ability to give a No-Cause Notice to a problem tenant. In the past, landlords could use No-Cause Notice to prematurely end a lease to get rid of a tenant that was causing a bad situation. Now you have to give a cause, and often a tenant can cure that cause (like a pet violation) and the tenant gets to stay.

No-Cause Notices

Landlords can serve a 30-day non-renewal notice to a tenant if the tenant still is within the first year of the lease. Otherwise, No-Cause Notices are now prohibited. As an example of this situation, I was recently contacted by someone who had heard me on the radio; he was unaware that Senate Bill 608 had recently passed. He wanted to sell a single-family residential rental property.

He gave the tenant a No-Cause Notice and told him that he (the tenant) had to move. Shortly after that, the tenant notified this landlord he had violated the new rent control laws, and the tenant was suing the landlord. The landlord told me that he knew the tenant had been coached by an attorney; he was fearful about what to do next. I told him at that point, he needed to contact an attorney and receive the right advice on how to protect himself, but it was a situation created because he didn't know he had violated the law, which meant he was in defense mode. The new tenant-landlord laws have painted a target on the back of landlords.

If you unknowingly violate the law, your tenants are often aware of their rights, and they will come after you. Be aware and be knowledgeable. If a No-Cause Notice is allowed, certain cities like Portland and Bend have specific requirements; the notice must be 90 days or longer. Eugene is the same way. Portland laws are very complex and have specific requirements related to notices and relocation fees. A landlord needs to understand the laws for the city where they own property to protect themselves. It's important that you consult with an attorney if you are in doubt about what is and isn't allowed.

A Criminal Record and Poor Credit

On June 19th, 2019, the Portland City Council voted three-to-one to adopt new policies intended to make landlords more forgiving of criminal records and poor credit when conducting the first screening of new tenants. The new tenant-screening ordinances now state: A landlord cannot reject applicants who had an arrest that didn't result in a conviction, or an underage conviction. Also, a landlord cannot reject applicants who received a misdemeanor conviction sentence three years before the housing obligation or housing date, or, more importantly, a felony offense conviction in which the sentencing happened seven years before the application.

One of the other interesting ordinances passed by the city council states: A landlord would have to consider a credit score as low as 500. If you look on Experian, it shows the average American has a credit score of around 695. According to Experian, a score of 500 is a very poor credit rating. In my opinion, landlords will now be required to take tenants who have lower credit scores than the landlord's desired screening rules, but the new rules will indicate and mandate they must now accept that tenant.

The Portland Housing Bureau is now drafting the official rules for this policy. The rules will add a litany of rental protections and housing regulations to apartment owners. I find many of my apartment owners who have been self-managing their units will now need to consider hiring a property manager to protect themselves. I will talk about why that's important a little later.

Undercharging on Rent

Recently, I took a call from a residential real estate broker who was listing a duplex for an out-of-state investor. The property manager had not kept pace with current market rents, and the broker wanted to raise rents to market rate before the property was listed for sale. The rents for each side of the duplex were $650, but market rents for the area were $895 per unit. The increased rents could have made a substantial difference in the owner's sales price had they kept pace with the market for rent. Unfortunately, you cannot raise rents to market just because you are selling the property. And you cannot give that tenant a No-Cause Notice and ask them to leave to make it easier to sell the property.

Many apartment complex owners who have quality tenants don't want to raise rents, out of respect for the tenants. As those multifamily owners try to sell their property, they see that situation potentially affect the value of the property they might receive when they prepare to sell, because their rents are below market cost. As rent control was about to be passed statewide, many owners rushed to increase their monthly rents, so many tenants received notices their monthly rent would increase almost $400 a month. While the state legislators thought they were benefiting the tenants by establishing regulations about future rent increases, I feel it hurt a lot of tenants because many tenants received a notice their rent would be raised before the new law went into effect. Some of the increases were large enough that it forced tenants to move and find cheaper places to live.

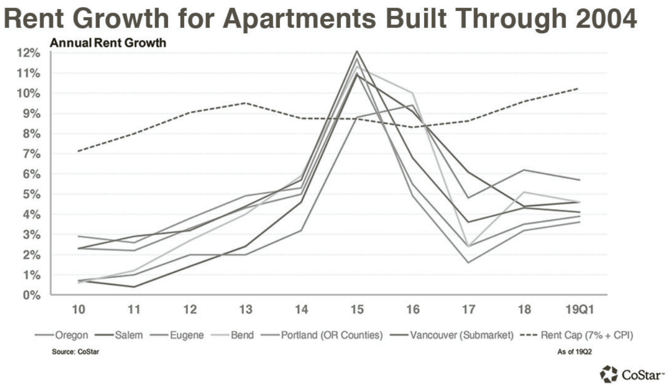
When those tenants moved, many investors decided (especially owners of one- to four-family properties) they would put the property on the market for sale. Rather than investors buying these properties, right now people are buying to owner-occupy those properties and moving into them as their residences.

It's taken more of the properties away from the available rental pool; especially in the Portland market, it has put a pretty substantial damper on available rental properties. If a property is 15 years or newer, rent control does not apply to those properties; however, the rents are substantially higher. As an example, a one-bedroom apartment in Portland could be rented anywhere from $1,500 to $3,000 depending on the apartment's size, amenities, and location. For many renters, this creates a financial burden and often leaves them with few options. The effects of rent control have backfired.

While it's great for the people who are buying the properties that are hitting the market as their personal residence, it's taking away the market share of available and affordable rental properties. Not everybody can afford to move into one of the new properties that are available on the market and the top rents. Many renters need more of a workforce-rent level. We are already seeing rent control have an impact on out-of-state investors' appetites, wanting to come in and buy new rental properties in Oregon, but also creating more of a housing shortage of available properties to rent.

Chapter Three: What You Need to Know About Rent Control

In the past decade, it was unusual for a landlord to raise the rent by more than 10 percent in a given year. Typical rent increases in Oregon were more around 5–7 percent. Occasionally, you would see a larger increase, but that was typically an isolated situation in which the owner had completed substantial renovations to the unit to support the increase. According to Emily Andrea, a leading analyst at the CoStar Group, if you look historically at the major rental markets in Oregon since 2010, rental growth has been far below the level set by the rent caps. An exception is shown in the peak of rent increases from 2015 to 2016; a chart is included on the following page. Reduced out-of-state buyer appeal will lead to erosion in market prices paid for in-state real estate.



What Causes This Reduced Appeal?

The problem with rent control is out-of-state buyers are concerned about buying in Oregon not knowing what future issues may arise from laws passed by legislators related to rent control. Uncertainty erodes the value investors seek in property ownership.

Using CoStar, I track multifamily property sales throughout the state of Oregon. It shows multifamily sales of market-rate properties, not affordable housing or government-regulated housing, but the market rate in which the average investor buys or sells those properties. Comparing those sales in March and April of 2018 against those of March and April of 2019, we see a 48 percent decline over those two periods. For all of the Oregon multifamily property sales in 2018, about 18 percent of that sales volume came from in-state buyers.

By contrast, about 50 percent of the buyers in the market were from California. Since many investors from California are familiar with rent control laws, they may continue to buy in Oregon, but I have serious doubts and concerns given the shift in attitude towards rental control and the new rent ordinances.

I recently talked to one of my investors out of Chico, California, who has bought several properties in the local area in the last 24 months. Earlier this year, he indicated they had substantial liquidity (cash) to invest and wanted to buy a multifamily property, but now with the recent ordinance passed by the City of Portland regarding the new screening laws, his appetite for buying in the state of Oregon has cooled. He's decided just to wait and see what's coming down the road for statewide screening laws and is now buying properties in other states. Why is this a concern?

Oregon Multifamily Sales Volume

March & April 2018	**March & April 2019**
$183 million	**$95 million**
50 Assets Sold	40 Assets Sold
Biggest Deal: $55 million	Biggest Deal: $7.8 million

Investment Decline:
48%

CoStar

Here's the danger: Investors are concerned that Oregon lawmakers could make the regulations more restrictive or reduce the current 7 percent rent control in the next round of legislation. There's no assurance the legislators will not make continual changes, and there are rumblings that Oregon legislators are going to reduce the 7 percent again. Many investors are concerned rent control could be visited over and over, and eventually reduce the amount down to a level where it wouldn't make financial sense for a multifamily investor to own property in Oregon. That has already happened in the San Francisco area, and in several other cities where they started at higher rent caps; the caps kept dwindling, I believe right now San Francisco is around 2 percent rent cap. If that trickles into Oregon, that would further reduce the appetite of investors who want to come in and buy property from out of state. With every new restriction of landlord rights passed by the legislators, it's driving away more and more potential out-of-state investors out of market. Fewer investors looking to buy will create less of a demand for your property if you decide to sell.

There are four carve-outs in the new state rules that would allow landlords not to renew a tenancy after the first year. If the owner is selling the property so that it will become owner-occupied, you can notify the tenant they must move out, and you give them notice. If you are planning to make major renovations or rehab a unit, you can give a tenant a notice of 90 days and tell them they have to move, as long as there are no other available units in that apartment complex. But you should only do that if the unit is uninhabitable, which would normally include the lack of a working bathroom or kitchen. This can't be a situation where you'd like to do a little painting and put in new carpet. It must be a substantial renovation.

What You Can Get Away With!

An investor called me recently after hearing me on the radio, and he wanted to know the minimal amount he could get away with on renovations. In talking to him for a few minutes and listening to his situation, it was obvious he wanted to paint and put in new carpet, and I advised him not to do that because that would be a violation of the landlord-tenant law.

Now, don't get me wrong, I'm not an attorney, and I don't give people legal advice, but I knew enough to know he was not going to make that unit uninhabitable; he was trying to upgrade it, and ultimately he wanted to raise the rent. I advised him to contact his attorney for future advice. But I told him if I were in his shoes, I would not do that.

The third carve-out is if you or an immediate family member planned to move into the unit. The fourth is if you plan to demolish or tear down the unit; if you plan to convert it to a condo, you are allowed to give the tenant notice they need to vacate and then you can move forward. If you decide not to renew a rental contract or give the tenant notice, you must state the reason for the termination. Many owners are interested in using one of these four carve-out rules as multifamily owners are always looking for a value-add opportunity.

If you're thinking about buying an apartment complex and rehabbing the units, and you want to increase the rents, know that you must make sure the unit is not habitable. Also, you need to be prepared to pay the tenant one month's worth of rent when you give them notice. That gives the tenant the money to find a new property, a new place to live, and pays their fees to move. Landlords with ownership in fewer than four properties do not have to pay that one month's worth of rent.

Also, *relocation fees are required* in the Portland area. If you own property in the Portland Multnomah area, you need to find out the exact requirements if you are unsure. Penalties for terminating a tenancy after the first year of occupancy, and violating Senate Bill 608, will subject the landlord to paying three months of rent and actual damages sustained by the tenant, as well as attorney fees and legal costs for the tenant. In my opinion, it also makes you liable so you will have to defend yourself against eviction action you might have put into place against that tenant.

Where Rent Control Doesn't Apply

While rent control applies to properties 15 years or older, it does not apply to government-subsidized buildings. Developers argue rent control plans are discouraging them from building new apartments. In 2017, the city of Portland was the first to pass rent control. At the same time, they passed an inclusionary housing requirement that requires any new construction of 20 units or greater to include a minimum of 20 percent affordable housing in that project. Developers started nixing large development projects in Portland that no longer made sense once they were required to have the 20 percent affordable housing and offer substantially reduced rents.

The state of Oregon must continue to measure the impact of rent control and watch to see if it will increase or decrease future construction. Again, we have a shortage right now in our market, so it's important to have state oversight to make sure developers continue to build. On my website, at the top of the page, there is a bright red button that says "Rent Control." You can click on there to read Senate Bill 608 and see the latest information available regarding rent control.

Chapter Four: Do You Need to Hire Professional Property Management?

A professional property manager can help an owner ensure their tenants are notified properly of any rent increases, while also ensuring the tenant knows the landlord's rules and the causes for eviction. The law states that if a tenant violates their landlord's rental rules three times in 12 months, you an evict them (three strikes, and you're out). If you are wondering if you can give the three notices all at the same time, the answer is no.

As an example, if you show up and your tenant is having a party, and there's underage drinking, and there are 50 people there, you cannot give your tenant three notices all at the same time. You can only give them one violation at that time, counting as one of the three-strikes-you're-out rule. A few days later you could do a walk through (with proper written notice), and go back and check the property for rental agreement violations. Things like missing batteries in the smoke detector, etc. If you are self-managing your property, you need to document and notify your tenant of each of their violations and the time the violation occurred.

The other violation that most landlords do not know that they can use to evict a tenant is regarding late rent payments. Rent is due on the first and you cannot charge a late fee until the fifth day. Typically, a grace period is written into rental contracts; it says if the tenant is late, there is a five-day window in which they can get the rent to the landlord and pay a late fee. But technically, the rent is due on the first, so the tenant has violated the rental agreement if you have not received the rent by the first of the month. I know several landlords who are now dealing with troubled tenants; the landlords are documenting when they receive the rent. If they have not received it by the first, they write that up as a violation of the rental agreement and notify the tenant. They plan to continue watching until they collect three violations and are able to terminate that tenant.

Not Everybody Is Bad

Not all tenants are bad tenants. Most tenants are respectful; they just want a great place to live and most pay their rent on time. But there are those occasional times when you will have a difficult tenant who is not taking care of your property. You have to be savvy in knowing how to deal with that. I know a lot of multifamily property owners who have managed their units for years, but given the severe penalties that apply to property owners if they violate the current landlord-tenant laws, I think it would be wise for most people to consider hiring a professional manager. The current laws state if an owner violates the law, you owe three months' worth of rent plus attorney's fees to the tenant.

I recently received a call from a property owner who had given improper notice to his tenant. The tenant then indicated he planned to sue the owner for three months' worth of rent plus damages; the tenant said he now was under stress and was unable to work. So that tenant may sue the landlord for missed time at work. Since the landlord didn't realize he had given improper notice to the tenant, he has to hire an attorney to defend himself. Had he hired a professional property manager upfront, the manager would have known how to give proper notice to ensure no violations would have occurred.

The Power of a Good Property Manager

A professional property manager will help ensure your tenants are notified of any rent increases, and will ensure that you do not exceed the current 10.3 percent limit on annual basis. They will also tell your tenant under which rules they can be evicted while making sure your property is cared for properly. A good property manager will also help owners establish market rental rates, collect monthly rents and deposits, advertise and market your property, and help you find good quality tenants.

Investors often tell me that they are worried about changing property types and going from multifamily to commercial real estate like leased office or medical type buildings. One of the benefits of going into commercial real estate is that you do not have to deal with any of the rent control rules. Many of my clients own property with a single national credit tenant as the tenant. Over the years, they have transitioned out of multifamily property by doing a 1031 tax-deferred exchange. They have traded up to commercial property so they can get away from dealing with tenants, and they got into a property that generates positive cash flow, gives them a more stable, economically viable opportunity because it's not tenant-based. They're also not regulated by the state.

There are a wide variety of commercial properties. The most common types are office, retail, medical buildings, and industrial. All of these properties come in different sizes and tenant mixes. Some office and industrial buildings only have one tenant and others have multiple tenants. I have received a lot of calls from Oregon property owners who own a duplex or two and want to 1031 exchange into commercial property. That is a little tough to do because the average price point to buy commercial real estate (where a tenant is in place making rent payments) typically starts around $850,000 to $1 million, and a 35 percent down payment is needed to get a loan. While you may have owned the duplex free and clear, now you will have high leverage on the property and most of the cash flow will go to service the debt on the property. I am not saying it cannot be done, but investors with smaller properties may want to consider other options.

Where I have seen good success and helped many clients is where a multifamily owner sells multiple smaller properties at the same time and then we 1031 exchange into commercial real estate. Several of my clients who have done this have found really good deals where they have a single commercial tenant with a nationally backed lease. Most properties that have a national credit tenant also have a triple net commercial lease (NNN), which means the tenant pays for property taxes, insurance, and most of the maintenance and repair on the property. The tenant pays for any future increases in property taxes and operating expenses, which will continue to increase over the years. These would be a few examples of a national credit tenant with a triple net lease: Walgreens, DaVita or Fresenius Dialysis Clinic, AT&T, Verizon, Starbucks, 7-Eleven, or a Dollar General, just to name a few.

When you are initially looking at a commercial property and are trying to decide if the property will meet your investment strategies, one thing to consider is the financial strength of the tenant. You can usually look up national credit tenants (their earnings and their credit rating) online because the company is publicly traded. This shows you the company's financial capacity to continue to make rent payments in a volatile market.

National credit tenant leases usually feature a corporate guarantee to the landlord. This ensures if they vacate your building prior to the end of the lease, the corporation backing the lease will continue to pay rent until the building can be re-leased. National credit tenant leases are often part of a sale-leaseback situation in which the tenant was instrumental in picking the location and agreeing to the specified rent period. These leases are often 10 to 15 years with rent increases included in the lease.

Many tenants will identify a desired location and coordinate with a developer to build a building for them, which is called a build-to-suit, in anticipation of the building later being sold to a passive investor and the tenant remains as the long-term tenant. This is nice for the investor because you're not building an empty building and then trying to figure out who will move into it.

The site location has been selected upfront by the tenant, who hired the developer to build it to their specifications; then right before they move into the property or as they're moving into the property, that property is then sold to a passive investor. From the passive investor standpoint, it is a great opportunity: they have a building (typically brand-new), which has a 10- to 15-year corporately guaranteed lease, and they've got a good, stable, long-term tenant in place.

Corporate Guarantees

I always recommend my clients look at all aspects of a property to make sure it will meet their expectations. One thing I like about most single-tenant lease situations is the corporate guarantee. It gives the owner peace of mind that the rent payments will be in the mailbox, regardless of what is happening in the marketplace. The other nice part is there's less involvement with tenants and typically less contact from the tenants. You may talk to the onsite tenant once or twice a year, but overall it's far less involved as compared to multifamily properties.

As an example, I'm currently helping a client with her Portland multifamily portfolio; she's selling three properties that were built in 2014, and she will be doing a 1031 exchange into a dialysis clinic. The Portland laws are pushing her out of the multifamily business, even though her properties have been well maintained. She's tired of dealing with tenants and knows that the screening laws will only make it more difficult for her to find good quality tenants. She has self-managed up to this point and has enjoyed doing that, but now she has decided the time is right to get out of the market. She's worked hard to build her portfolio, but the handwriting is on the wall, and it's only going to become more difficult as Portland passes more ordinances favoring the tenants.

I prepared a commercial property evaluation to show her the most probable sales price of her properties, and we looked at the equity she had available and the cash flow she was trying to generate as part of her strategy going forward into a new property. She was hoping to find a property with no residential tenants and one that would require less of her time. Because my client knew what her most probable sales price would be based on my analysis, we listed the properties at the price I recommended. They sold within 24 hours. We received full-price offers, which she accepted; she even had multiple backup offers shortly after we listed them. Imagine the luxury of knowing you have a backup offer, giving you peace of mind as you deal with that buyer and wait for the transaction to go through. If something happens with the first buyer, you can always go to the backup buyer. It puts you in the driver's seat during the selling process. It doesn't always work that way, but it's nice when the demand is there, and you can receive a backup offer.

My client asked me to help her find a good replacement property for her 1031 exchange that would offer steady monthly income while releasing her from dealing with residential tenants and would require less of her involvement as the property manager. We discussed several options and different real estate types, including leased office, leased medical, retail strip centers, and more multifamily properties outside the state of Oregon.

And the Winner Is…

She had lots of options but ultimately decided to purchase a new building with a single tenant in the building and a lease offering a corporate guarantee. The building is a brand-new state of the art medical building and was built for a dialysis clinic. The tenant found this location was important due to the proximity to the hospital, the demographics of the growing community, and lack of other kidney dialysis clinics in the area. The tenant signed a 15-year corporate-backed guaranteed lease agreement. They also installed over $2 million worth of tenant improvements in the interior of the property. This gives my client peace of mind: the tenant has a very high likelihood of renewing their lease at the end of 15 years because of the improvements they invested in this property.

The tenant is in the business of medicine, not in the business of owning and managing real estate. They want to operate a kidney dialysis clinic and treat patients. That's why they found the location where their highest demographic was for the patients who needed services. They approached a developer to build the building for them; they knew day one that they would sell the building to a passive investor so they would not own the real estate. When the building was complete and they prepared to move in, they asked the developer to help them find a buyer that would come in and purchase the building from them.

That's where my client was able to find this great opportunity to get out of multifamily property and into a single-tenant situation. There are lots of opportunities (single tenant properties for sale) like this all over the United States. They are properties that you and I drive by every day: Jack in the Box, Advance Auto, Jiffy Lube, Applebee’s, Verizon, and so forth. There are lots of options out there if you are wondering what you would do with your multifamily portfolio.

My client was also able to secure very competitive financing terms. Lenders like properties that offer corporate guarantees and feature a national credit tenant; typically, they will work hard to win your business by offering attractive financing terms. I work with knowledgeable lenders who specialize in commercial real estate and have experience in closing these types of transactions as well as multifamily transactions. My goal is to be a great resource for you and refer you to the people who can help you in your current situation. Whether it is a lender, property manager, or good real estate attorney I can refer you to the people who can help get the job done.

Chapter Five: Issues that Will Affect Oregon Property Investors

A market disruptor can be viewed as good or bad, but it should be observed. Every year, the counselors of real estate issue a list of the top 10 issues that affect commercial real estate. This year, the list included:

1. Weather and climate-related risks, wildfires, and floods
2. Infrastructure
3. Housing shortage in America
4. The technology effect
5. End of cycle economics
6. Political division
7. Capital market risks
8. Population migration
9. Volatility and competence
10. Public and private indebtedness

Some of the biggest things that will have an impact on state and national real estate markets include the statewide rent control already reviewed. There are trends of state and local taxes increasing, the Oregon PERS Retirement deficits, rising interest rates, and the economy. Other factors include political uncertainty with terrorists and different areas regarding relationships with China and other countries, end-of-cycle economics, affordable housing crisis, and the level of risk willingly adhered to by the capital market lenders. Read any newspaper or news feed and you can see the strife that we are in on a national and international level.

Real estate demand is derived from the economy, and many signs show the expansion could be ending in 2020. Interest rates and the federal reserves started to signal trouble when the yield curve inverted in March of 2019. The inverted yield curve proves investors are bullish on the short term but are concerned about the long-term health of our economy, primarily due to mounting public and private debt. According to a recent article in Reuters, U.S. household debt in America is more than $13.3 trillion. NPR stated that U.S. national debt hit a new record level of $22 million; that is a concern for foreign investors looking to bring capital into America.

On a state level, Oregon's public pension system is also in a crisis. The Oregon PERS' unfunded liability grew by $4.3 billion to a whopping $26.6

billion last year. Its funded status declined from 73 cents to 69 cents and assets for every dollar in liabilities. The anticipation is the deficit will increase closer to $29.2 billion in 2019. According to a recent article by the Oregonian, this illustrates how difficult it will be for Governor Kate Brown to deliver on her pledge to hold pension costs constant for schools and preserve any new revenues from a corporate tax increase for schools.

Property Tax Increase

In April of this year, one of my clients emailed me an article about a proposed Oregon property tax increase that was rather alarming. At the beginning of 2019, the legislature was considering taxing properties for commercial and industrial purposes based on the properties' real market value instead of the way Oregon properties are currently taxed, which is on land value. For many of my clients, this would have raised their property taxes by 30 to 40 percent. Luckily, the bill was killed before it was even debated, but it doesn't mean the legislators won't try to bring it back in the future. The governor and the legislators have a big job ahead of them trying to balance PERS and the budget, and the question remains whether they will try to take a swipe at commercial property owners to balance the budget.

The end of the real estate cycle is one of the factors I watch in order to gauge what will be happening for multifamily and commercial property owners in Oregon. Right now, money is still free-flowing, and interest rates are low, but capital markets adjust quickly with the adjustment of the bond market, and lending options can dry up quickly. As interest rates rise, market saturation occurs, vacancy rates creep up, and out-of-state buyers potentially start looking to buy in other states.

The real estate market in Oregon could change quickly, and property values could change with it. As an example, I personally own an apartment complex with my husband and those proposed property taxes (that could have been raised by 30 to 40 percent) would have increased from $15,000 to $25,000, which makes a substantial impact on the net operating income.

Some strategies to protect your investments are:

1. Get informed.
2. Lobby your legislators.
3. Join your local housing association.
4. If you own multifamily property, become a member of your local landlord housing association. Multifamily Northwest (www.multifamilynw.org) is an organization designed to represent multifamily owners in the state of Oregon. They provide the latest updates and information that will impact multifamily

owners, as well as new state legislative changes that could impact you as a property owner and a multifamily owner. They also have the latest rental agreement forms available for purchase with the updated language pertaining to the new laws. I can't stress this enough: join an organization or group that will provide you with the information and knowledge you need as a landlord. It will be the best money you have ever spent—hands down!

Chapter Six: Positioning Your Portfolio for Future Growth

The biggest danger for you is to do nothing.

Doing nothing does not work because the landscape is changing around you. Most likely, you will be faced with bigger challenges in the future from higher interest rates and softer real estate value due to fewer buyers in the market, or as the real estate market cools off due to disruptions in the economy.

I am not trying to scare you. I am trying to inform you and provide information so you know what is happening. It can be a full-time job trying to keep track of the changes on a state and local level when it comes to multifamily. Many investors are concerned about the future but not sure what to do.

As one of my older clients told me this week, "My wife and I have talked about doing something with our multifamily [mainly duplexes] portfolio. We have worked hard building what we have. We see the changes coming and we don't want to be the last person out the door and lose substantial value in our properties because we didn't do anything."

Here is what I recommend you do right away: Identify the current market value of your property so you can make good future decisions. For serious investors, I offer a Commercial Property Analysis Report. My 14-page analysis measures the productivity of your property and shows you the most probable sales price, which allows you to decide what to do next. Using the Equity Optimizer Analysis, which is part of the report, you can measure the equity you have available to trade up in size or value.

The 1031 Exchange Calculator will show you the tax benefits of using your sales proceeds in a 1031 exchange, including the sales proceeds before taxes and after taxes. The benefits of my Commercial Property Analysis are:

- Identify annual tenant income
- View vacancy rates and rent trends
- Measure the last three years of your property's operating performance
- Review your cash-on-cash Return

These are some questions we help you answer:

- Do you need to add more property to your portfolio to create more income?
- What type of property will provide you with the income you are looking for?
- Do you need to consolidate smaller properties into one or two larger properties? (This helps free up your time and gives you less of a management headache.)
- Do you need cash flow for future health concerns?
- Do you need to create generational wealth for your kids or your grandkids?
- How can you take advantage of new opportunities and a changing market?

One thing we also help you with is to weigh and examine your leverage; be leery of leverage. Being over-leveraged can sink your ship in a declining market. I always recommend my investors put at least six months of reserves aside in case the rental market softens. Also, you should know what commercial lenders are looking for in safety features when they're reviewing a portfolio. If you want to seek new investment opportunities to grow your portfolio, you need to talk to a lender to know your buying capacity.

The lender may ask you for a resumé because they're looking for your years of experience in owning commercial real estate. Paint a picture for them and give them as much detail as possible. Lenders may ask pointed questions of their own:

- How much debt do you have?
- Are you improving your cash flow situation?
- Do you have experience in owning this property?

You don't want to make a bad decision because you didn't have all the facts. You want to understand your options and know what you are doing. Schedule a free 15-minute Discovery Call with me to discuss your options. We can discuss ways to help you generate more wealth in the future that will create less work for you. It's my goal to be your guide, to help you see the options available to you, and to help you understand how you can improve your current situation.

As an example, I recently helped an investor using my Commercial Property Analysis. We looked at her portfolio of single and multifamily properties and how she could do a 1031 exchange into leased commercial real estate to get out of dealing with residential tenants. She's experienced health issues in the past and wanted more ease of management, but she needs dependable income from her real estate to fund her lifestyle. Through my Commercial Property Analysis, I was able to show her how she could

1031 exchange those properties into one property; that way, she could have better buying capacity to buy one large commercial building. It created a larger positive cash flow for her because the tenant is responsible for the maintenance and repairs on the building, plus property taxes and insurance.

She can now enjoy a steady stream of consistent, reliable income without having to deal with residential tenants and the day-to-day stress of self-managing her properties. She was relieved to know she had options and that she didn't need to get out of real estate as she ages. She just needed to trade up into commercial property for benefits that fit her lifestyle and long-term financial needs.

Final Thoughts

Our current market disruptors will impact property values. As an Oregon real estate investor, you need to know your options. As a savvy investor, you want to understand what is available to you as well as the best strategy, but you also want to understand options so you know you're making the right decision. My Commercial Property Analysis Report can show you how you can defer taxes by using a 1031 tax deferred exchange, including your before tax and after tax benefits if you decide to trade up to a different property.

You bring many strengths to the table as an investor. You understand multifamily properties and have done well with your portfolio. Many investors are curious about other commercial property opportunities. You need to see what options you have to trade up in size or value.

My Unique Process

This is how I can help you. First, we meet on a free 15-minute discovery phone call. Go to my website to schedule this free initial phone call: **www.DisruptorsinOregonRealEstate.com**. If we're a good fit, then we have a 30-minute real estate strategy meeting by phone or in-person to discuss your options. You supply me with the last three years of your operating history (Schedule E's or 8825s if you own your property in an LLC). Next, we design a Commercial Property Analysis Report for you. We meet with you to review your plan and discuss your options. If you want to move forward, we create a timeline and develop a game plan. We assist you in finding a new property if that's part of your plan, and we help you close the transaction.

I recently had a client ask me about selling multiple properties. On our initial 15-minute phone call, I heard what she wanted to do, and I knew I could help her. I asked her to send me a current rent-roll, and the last three years of her Schedule E tax statements for each of her properties. That way, I could analyze the amount of cash she would be able to harvest out of those properties when she sold them, and what the value of those properties would be. After reviewing her portfolio, I was able to give her some ideas of different properties she could tap to hit her income goals, as well as ease her out of the day-to-day management that had become so labor-intensive.

When we reviewed her options, I explained to her the benefits she would see by going into these new properties. She then decided to sell those properties and 1031 exchange into a new property. One of the reasons investors want to look at options may be their financial situation: they may want to grow their income and their portfolio. Perhaps your age is now indicating that you need to make different lifestyle choices due to retirement or declining health. I have many investors tell me that their stamina to work on their multifamily properties diminishes with age. Add some stress to that with dealing with terrible tenants and you may wind up with bigger health issues or wonder if there is light at the end of the tunnel.

Family dynamics can also come into play and be part of the decision for an investor on what they do next with their apartment portfolio and whether they move into commercial real estate. Many of my older investors built their multifamily portfolios as boot strap investors. They got into their first units with little cash, worked hard and put in a lot of sweat equity and grew it from there.

They have spent years building this portfolio. Their kids were not involved in the day-to-day operations of the portfolio, and now the parents want to look at opportunities to pass the portfolio onto the kids upon their death but don't want to leave them with a big headache.

Transitioning into leased commercial property with a solid tenant in place may make the most sense for investors weighing those decisions. If you give your kids a property that has a long-term lease and generates cash flow, they will be more likely to keep it then sell it and squander the cash away after you are gone.

I know there's a lot to analyze and determine and weigh out. I offer serious investors a no-cost analysis of their situation. It will show you the best type of property for you and what your investment strategy should be in order to survive market disruptions, which could impact the property values you currently own.

Here's How We Can Help You Survive Issues Impacting Oregon Real Estate Investors and Property Owners

Oregon multifamily owners are frustrated and confused about their options. Rent control and the new screening laws have moved the needle in favor of the tenant. Many landlords are fed up with the government telling them what they can charge for rent. These new laws have painted a target on landlords' backs if they make a mistake. A landlord is liable for three months of rent plus damages (tenant's attorney's fees) if they make a mistake. As a savvy investor, you want what to understand your options, and you want to know that you were treated fairly.

We put you in the driver's seat of your real estate portfolio. We help people just like you stay up-to-date with the laws and regulations governing your properties. Here's what you do next:

Step 1: Go to my website **www.DisruptorsInOregonRealEstate.com**.

Step 2: Click on "Schedule a free Initial Discovery Phone Call" button.

Step 3: Fill out my easy intake form.

Step 4: Be prepared to discuss your scenario during call.

It's your real estate portfolio, purchased with your hard-earned money. Let's make sure your investment is working as hard for you as you worked for it!

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