



COMMERCIAL REAL ESTATE INVESTING

A Creative Guide to Successfully Making Money

DOLF DE ROOS

Author of the *New York Times* Bestseller, *REAL ESTATE RICHES*

COMMERCIAL REAL ESTATE INVESTING

A Creative Guide to Successfully Making Money

DOLF DE ROOS



John Wiley & Sons, Inc.

COMMERCIAL REAL ESTATE INVESTING

COMMERCIAL REAL ESTATE INVESTING

A Creative Guide to Successfully Making Money

DOLF DE ROOS



John Wiley & Sons, Inc.

This book is printed on acid-free paper. (∞)

Copyright © 2008 by Dolf de Roos. All rights reserved.

Published by John Wiley & Sons, Inc., Hoboken, New Jersey.

Published simultaneously in Canada.

No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means, electronic, mechanical, photocopying, recording, scanning, or otherwise, except as permitted under Section 107 or 108 of the 1976 United States Copyright Act, without either the prior written permission of the Publisher, or authorization through payment of the appropriate per-copy fee to the Copyright Clearance Center, Inc., 222 Rosewood Drive, Danvers, MA 01923, (978) 750-8400, fax (978) 646-8600, or on the web at www.copyright.com. Requests to the Publisher for permission should be addressed to the Permissions Department, John Wiley & Sons, Inc., 111 River Street, Hoboken, NJ 07030, (201) 748-6011, fax (201) 748-6008, or online at <http://www.wiley.com/go/permissions>.

Limit of Liability/Disclaimer of Warranty: While the publisher and author have used their best efforts in preparing this book, they make no representations or warranties with respect to the accuracy or completeness of the contents of this book and specifically disclaim any implied warranties of merchantability or fitness for a particular purpose. No warranty may be created or extended by sales representatives or written sales materials. The advice and strategies contained herein may not be suitable for your situation. You should consult with a professional where appropriate. Neither the publisher nor author shall be liable for any loss of profit or any other commercial damages, including but not limited to special, incidental, consequential, or other damages.

For general information on our other products and services or for technical support, please contact our Customer Care Department within the United States at (800) 762-2974, outside the United States at (317) 572-3993 or fax (317) 572-4002.

Wiley also publishes its books in a variety of electronic formats. Some content that appears in print may not be available in electronic books. For more information about Wiley products, visit our web site at www.wiley.com.

Library of Congress Cataloging-in-Publication Data:

de Roos, Dolf.

Commercial real estate investing : a creative guide to successfully making money / Dolf de Roos.

p. cm.

ISBN 978-0-470-22738-1 (pbk.)

1. Commercial real estate. 2. Real estate investment. I. Title.

HD1393.55.D47 2008

332.63'24—dc22

2007039477

Printed in the United States of America.

10 9 8 7 6 5 4 3 2 1

Contents

Preface		xi
Acknowledgments		xiii
Notes on Reading This Book		xv
Introduction		xvii
CHAPTER 1	Just What Is Commercial Real Estate?	1
CHAPTER 2	People versus Contracts	5
CHAPTER 3	Why Invest in Commercial Real Estate?	11
	Lease Duration	11
	Assignment of Lease	15
	The Tenants Pay the Outgoings	17
	Tenants Earn Their Income on Your Premises	18
	Landlord Pays for Improvements to Commercial Premises	21
	Certainty of Collecting Rent	22
	Upward-Only Rent Reviews	24

vi Contents

	Government Interference	25
	Management Overhead	27
CHAPTER 4	The Downside of Commercial Real Estate	29
	Much More Difficult to Acquire Commercial Tenants	29
	Banks Will Lend a Smaller Proportion of a Commercial Property	30
CHAPTER 5	The True Value of Real Estate	33
CHAPTER 6	How to Overcome the Disadvantages of Commercial Real Estate	41
CHAPTER 7	How to Attract a Tenant	45
	Who Wants to Run a Funeral Business?	45
	Finding a Tenant for a Warehouse in an Oversupplied Market	50
	The Power of the Internet	55
	Many Prospective Tenants Know Your Building	56
	Engage a Real Estate Firm or Property Management Company to Find a Tenant	59
	Wait for (or Cause) a Zone Change	60
	Split a Single Tenancy into Multiple Tenancies	62
	Consolidate Multiple Tenancies into One	64
	The Ultimate Way to Attract a Tenant	66
CHAPTER 8	How to Increase Rental Income (and hence the Capital Value)	71
	Helipads	72
	Cell Phone Towers	73
	More Rooftop Antics	74
	Naming Rights	76
	Air Space	77

	Parking	81
	The Humble Webcam	89
	Interior Remodel	93
	The Triple Win of Alarm Systems	100
	Rent Reviews to Market	101
CHAPTER 9	What Were the Disadvantages of Commercial Real Estate?	103
CHAPTER 10	Finding Commercial Real Estate	107
	Newspaper Advertisements	107
	Real Estate Firms	112
	The Internet	114
	Keeping Your Eyes Peeled	116
	Networking	118
	Word of Mouth	118
	Helping Other People	124
	The 100:10:3:1 Rule	126
	Summary	130
CHAPTER 11	Analyzing Deals	131
	Due Diligence	132
	Four Questions to Ask about Any Commercial Property	142
	Return on Investment	144
CHAPTER 12	Negotiating Commercial Real Estate Deals	155
	The Uncooperative Seller	156
	Other Negotiations	159
CHAPTER 13	Financing Commercial Real Estate	163
	Proposal for Finance	166
	Summary Paragraph	171
	General Description of Property Offered as Collateral	174

viii Contents

	Property Portfolio Statistics and Cash Flows	176
	Statement of Assets and Liabilities	177
	What to Include in the Appendix	178
	How to Use the Proposal for Finance	179
	Umbrella Loans	182
CHAPTER 14	Structuring Commercial Real Estate Ownership	183
CHAPTER 15	Managing Commercial Real Estate	187
	Tenant Selection	188
	Rule Enforcement	189
	Rent Reviews	190
	How to Get a Tradesman to Do Your Work First	190
	Accounting	193
	Summary	193
CHAPTER 16	How to Beat the Average	195
	Geography	196
	Zone Changes	199
	Proximity to Views	200
	The Center of Town	200
	High Technology	201
	Leasing and Management Tactics to Beat the Average	202
	Combining All Methods of Beating the Average	202
CHAPTER 17	Raw Land	205
	Best Choice Properties	208
	Spring Mountain Ski Ranch	211
	The Benefit of Having Great Partners	214
	Getting Back to Commercial Real Estate Investing	216

CHAPTER 18	Extraordinarily Odd Commercial Deals	217
	Oil in Them Thar Hills	219
	Marine Farms	222
CHAPTER 19	Property Ventures Limited	225
	Five Mile	230
CHAPTER 20	Never Sell	233
CHAPTER 21	Thirteen Golden Rules of Commercial Real Estate Investment	239
	Golden Rule 1: Risk Is Equal to Yield	239
	Golden Rule 2: Ensure Safety of Principal	240
	Golden Rule 3: Control Your Liabilities	240
	Golden Rule 4: Add Value to a Deal	241
	Golden Rule 5: A Broker or Agent Must Bring Something to the Deal	242
	Golden Rule 6: Real Estate Is a Long-Term Investment	243
	Golden Rule 7: The Number of Voting Partners Is Directly Proportional to the Failure of the Project	244
	Golden Rule 8: You Are Going to Be in a Lawsuit	244
	Golden Rule 9: It Only Takes One Deal to Go Broke	245
	Golden Rule 10: It Only Takes One Deal to Make a Million Dollars	245
	Golden Rule 11: The Value of a Property Is Limited by the Tenant's Ability to Pay Rent	246
	Golden Rule 12: Appreciation and Inflation Are Compounded Annually	246
	Golden Rule 13: You Cannot Give Kindness Away—It Is Always Returned	247

x Contents

CHAPTER 22	Investing Abroad	249
CHAPTER 23	Live Life to the Fullest	261
About the Author		269
Appendix: Resources		271
Index		281

Preface

Anyone with \$20 million in his pocket can go out and buy a \$20 million real estate portfolio. This book is not for those people—it is for those with little or even nothing in their pockets, who want to go out and make a fortune anyway.

Of course, if \$20 million is just a little to you, you can still benefit from this book and learn how to easily acquire \$200 million or more of real estate. In my experience, though, people with this kind of cash often do not have the time or inclination to do so. Therefore, those with no money and lots of drive may do well teaming up with people with lots of money and no inclination, to form a truly symbiotic investment partnership.

Beware, however, that your perception as to what constitutes a lot of money inevitably changes as you start to accumulate some. While this book focuses on how you can amass a fortune, remember that in a hundred years' time, how much you will have made will not be of much importance to anyone. In the final analysis,

xii Preface

how much fun you have along the way could be the ultimate reward. That is why I say, above all else, be curious, learn something new each day, help other people, be grateful, and have fun!

Successful investing!

Dolf de Roos

August 2007

Acknowledgments

My passion for commercial real estate has been inspired and fueled by many people. While my thoughts, theories, and methods have been formulated over many years, countless people have—wittingly or unwittingly—contributed to my thinking, from real estate agents, bankers, mortgage brokers, and appraisers, to tenants, members of real estate investment associations, accountants, and literally thousands of investors (both budding and experienced) who have honored me by attending my events and who have forced me to expand my thinking.

While it is impossible to acknowledge everyone, many people deserve and have my deep appreciation. If I have missed you, then I apologize in advance; know that my appreciation is real nonetheless.

Sincere thanks go to Jay Abraham, Anthony Aoun, John Baen, Wayne Bourke, James Burgin, Randy Carder, Stephen Collins, Allen and Kenina Court, Keith and Sandi Cunningham, Curt Denny, Ross Denny, Craig Donnell, Charles Drace, Cary Ferguson,

xiv Acknowledgments

Andy Fuehl, Paul Gibbard, Andrew Gibbons, Daniel Godden, Pepi Gomez, Anthony Gough, David Grose, Datuk Maznah Hamid, Laurie Harting, Paige Hemmis, Dave Henderson, Adrian Heyman, Ian Jackson, Larry Jellen, Bob Jones, Stefan Kasian, Cindy Kenney, Rich Lamphere, Patrick Liew, Dave and Vicki Lovegrove, Katie Moustakas, Nick McCaw, Wayne and Lynn Morgan, Mike Pero, Craig Peters, Neale Petersen, Kean Pitcairn, Jim Poignand, Carrie Putman, Trevor Quirk, Tony Robbins, Alex Rodriguez, Paul Roussel, Trevi Sawalich, Constantine Scurtis, Mike Sexton, Bill Shopoff, Scott Sullivan, Garrett Sutton, David and Julia Sykes, Richard and Veronica Tan, Brian Tracy, Donald Trump, Dr. Robert Tybon, Andrew Waite, Jon Ward, Tung Desem Waringin, Richard Watters, Ron Whiteley, and Paul Wright.

Notes on Reading This Book

Numerous photos are included in this book to illustrate properties being discussed or points being made. Because of printing constraints, these photos are reproduced in black and white. Full-color versions of these photos, as well as other supporting documentation, photos, and newspaper articles, can be found on the web site www.dolfderoos.com.

Many examples of real estate bought or negotiated are discussed, ranging in value from \$59,000 to hundreds of millions of dollars. As this book is intended for those who are relatively new to commercial real estate, an emphasis has been placed on using modest examples of properties that hopefully are within the comfort zone of most readers. Bear in mind, however, that the effort required to complete an \$80,000 deal is about the same as that required to complete an \$80 million deal, so do not intend to focus on smaller properties forever.

xvi Notes on Reading This Book

Finally, please accept that any instances of words like *he*, *she*, *his*, or *her*, unless specifically referring to a person of known gender, are generic. Sometimes it is too cumbersome to write “he or she” or “his or her portfolio,” but the points being made apply to anyone.

Introduction

If you think commercial real estate is just like residential real estate except that you need more capital to get started, you are in for a surprise. Commercial real estate is completely different and often requires little or no capital.

If you think, like the masses, that commercial real estate is risky because you have often seen vacant commercial premises and thanked your lucky stars that you are not the owner, you are in for a shock. For reasons that I am excited to share in this book, I *seek out* vacant commercial buildings, as I have figured out a way of making money, huge sums of it, seemingly out of thin air, by doing something very straightforward with these vacant buildings—*something that you cannot do with residential buildings*.

If you think commercial real estate is too complex, too specialized, too esoteric, and too difficult for you to even consider, then let me take you on a journey to convince you that it is none of these things. In fact, I firmly believe that after reading this book, you will no longer want to even consider residential real estate as

an investment option, and will focus instead on commercial real estate with both enthusiasm and confidence. The only regret you may have is that you didn't discover this information sooner.

Consider this: Of all the wealthy (\$100 million-plus net worth) property investors I have come across in over 30 years of investing and teaching real estate in more than 25 countries (I have had the privilege of working with many prominent people in real estate all over the world), at most two have made their fortune through residential property—the rest have all done it through commercial property.

Think about this. You wouldn't choose a surgeon with a low patient survival rate when there are others with a high survival rate. You wouldn't choose a car with a low crash-test rating over one with a high rating, or a school for your kids with a low graduation rate over one with a high graduation rate. So now that you know that nearly all wealthy property investors have achieved their wealth through commercial real estate, how can you justify even thinking of buying one more residential property? It would be like dropping your kids off at a bad school, and driving yourself in an unsafe car to a hospital to have surgery performed on you by a surgeon with a low patient survival rate. That is nuts, right? Well, in relative terms, so is investing in residential real estate.

This last fact alone should be enough to convince you to convert to commercial real estate, and you could save yourself a lot of time by not having to read the rest of this book if you converted on that basis. However, you would miss out on a lot of fun, which brings me to my next point.

If you think commercial real estate is dry and boring, and the only reason you'd even consider it is that it is lucrative, then you are in for a real surprise. Residential real estate, for reasons I ex-

plain in this book, can be repetitious and therefore somewhat bland, but commercial real estate has so many opportunities for creativity, thinking outside of the box, and coming up with wacky ideas, that it genuinely is a lot of fun. At any rate, after I present my case, you can decide for yourself.

In case you think that I am contradicting myself and the 10 books I have written on residential real estate, think again. I stand by everything I have said in those books: Residential real estate truly is, in my opinion, a much better investment than stocks, bonds, mutual funds, Treasury bills, certificates of deposit, commodities, options, futures, and unit trusts, for reasons that I have explained in some detail in those books. However, when faced with a choice between residential and commercial real estate, I would recommend commercial real estate as your way to riches. Certainly, with my own investing, I have long ago focused almost exclusively on commercial properties, for reasons that I share in this book.

There are, of course, many ways of investing in commercial real estate, as evidenced by the number of existing books on the subject. You will find this book to be different. The fact that I have a different approach, philosophy, and strategy does not, however, invalidate others. You may successfully implement the ideas in this book, and you could also successfully implement the ideas of other commercial real estate books. (You may also be unsuccessful in either case, although it is difficult to fail in real estate as the market is so forgiving of tactical errors.)

At the end of the day, it is not just knowing a strategy, but how you implement it, that can be the difference between a successful experience and a learning experience. If you have an angry, gruff, stern, and rude nature, you could go on vacation to some exotic place and conclude that all the locals are angry, gruff, stern,