

Multi-Unit Apartments



By Brian Madigan

A number of clients will ask about multi-unit apartments. Are they good investments? Do they make sense? What's the cash flow? How do you manage tenants? And, more importantly, can I afford one?

So, let's have a look at a recent listing and see if the numbers make sense. As for the tenant issue, most people make good tenants, so you really just need to know how to find them. The bad tenants get all the publicity. Rarely, do you hear a story about a good tenant who pays on time.

Here are some of the **particulars**:

20 units
almost 1/2 acre of land
2 storey structure
about 30 years old
brick and concrete construction
26 parking places
hallways of terrazzo
wood floors in suites

Financing

asking \$ 1,850,000

assume first and second for \$ 1,500,000
cash required \$ 350,000 as in cash to mortgage (ctm)

Gross Income

gross income \$ 197,316
expenses \$ 76,613

More detailed Expenses

Taxes \$ 36,419
Insurance \$ 2,074

Gas (heat) \$ 9,910
Hydro \$ 8,455
Water \$ 6,273
Maintenance \$ 9,000
Superintendent \$ 1,500
Vacancy allowance \$ 2,000
Snow removal \$ 1,000

Total \$ 76,361

The cash flow

net (before mortgage payments) \$ 120,685

1st \$ 5,473.89 (p+i) monthly (interest rate 6.53%) due in 2 years

2nd \$ 1,744.81 (p+i) monthly (interest rate 5.00%) due in 2 years

net cash return \$ 34,061

plus (p paydown) \$ 19,260

Total annual return \$ 53,321

Analysis

So, a \$ 350,000 investment will yield an annual return of \$ 53,321.

Or, another way of looking at it would be to say that your income will return your cash investment in 6.56 years.

The income is 15.23% of your actual cash investment.

You should also know that financially you will not be able to mortgage the rest. In other words, you really need this \$ 350,000 as your downpayment. If you have it, then the numbers will work for you. If you don't, then the additional costs of financing will remove all of your profit.

On these types of properties most banks will provide up to 75% by way of a first mortgage. Secondary financing will provide a further 15%. So, in most cases, the amount of equity you will require will be 10%. Another way of looking at this would be that you would be generally able to acquire a property 10 times the value of your downpayment. The revenue stream from the building will be all the information that the lender requires. It's not like a residential mortgage that would be limited by your other income.

If you were to compare it to a GIC from a bank, you're likely to find that you will have about triple the return. In addition, the \$19,260 is principal paydown and it's not taxable. In fact, should you later withdraw these funds by way of an

increased mortgage, you will find that it will not be taxed at that time either.

You will be able to deduct your expenses for tax purposes and you will have to include your income. You will also be able to claim depreciation on the building at the rate of 5% per annum. When you sell, the increase in value will be subject to capital gains tax, unless you are considered to be “in the business” in which case, the increase in value must be reported as income.

While this is not intended to be an exhaustive list of what to look for in a multi-unit building, you will want to inspect the building carefully for any immediate repairs. In fact, you should set up a budget for capital replacements. Obviously, you should have the building professionally inspected.

When it comes to residential tenancies, you will have to look at the Residential Tenancies Act that came into force in January 2007.

Some investors like multi-unit apartment buildings and some don't. Others seek to acquire them in order to convert them to condominiums. There is usually a good profit if this can be done.

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