To all who have allowed me the opportunity to join you in your investment lives, I sincerely hope that this series of "White Papers" will be enlightening and even helpful in your continuing pursuit of profitable Real Estate investments.

The Rules of Real Estate Investing

GERALD GUTERMAN | SENIOR PRINCIPAL PARTNER, CHIEF INVESTMENT OFFICER

For all its rewards, Real Estate can be a treacherous business. Whether you directly purchase Real Estate for investment or elect to participate as an Investor or Limited Liability Partner with a Professional Investor or Investment Company, you are taking on responsibilities that require you to think and act like a professional. If you don't think and act accordingly, you may well be less than successful with the results your **"money"** is contemplating.

Let's look at one example of unprofessional behavior: the so called **"Rules of Thumb"** when making an investment sounds good to those without any in-depth knowledge, but generally they have no basis in fact, and they certainly do not impart wisdom.

Your money dictates that you must follow and live by certain **"Investing Rules"** to ensure survival and profit. These are not Rules of Thumb! These are in fact Rules of Pragmatic Actuality. Every Real Estate transaction is completely immersed in these pragmatic actualities, which are always governed by the same Rules that guide every investment.

A business and social friend of mine since 1978 continuously repeated the same words..."*location, location, location, demographics, physical condition, cash flow, financial history, stability and future resale value.*"

To those of you who have a sense of Real Estate history, my friend's name was Harry Helmsley, and he was married to another famous individual... Leona Helmsley. Harry is one of the most, if not the single most, successful real estate investor in United States history. Leona was famous for her operation and control of the Helmsley Hotels empire. If you want to have an enjoyable moment and an approving laugh, check them out.

From the beginning of our investing history, circumstances essentially demanded that we add to the factual accuracy of Guterman Partners investments. We decided early on, that in-depth demographic research prior to every property's acquisition was mandatory for successful operations. In the real estate industry, we are known as **"demographic geeks."** We believe that demographics are the **"lifeblood"** of Real Estate.

That said, ask any broker for a Demographic Summary and you will be surprised that less than one in one hundred even knows what you are talking about. If you want to really confuse them, ask for the ratio of disposable income per square foot in the demographic (potential renters or buyers) model to the average cost per net rentable/saleable square foot in the specific property and its competition.

If the property is in a family neighborhood, and the other aspects conform to the neighborhood, then ask them exactly what schools are servicing the neighborhood and the specific individual national **"rating"** for each school. Remember, desirability of a property and a neighborhood are significantly influenced by the quality of the amenities in the property and in the surrounding neighborhood. In a family area, the schools have the over-riding importance.

Due Diligence is mandatory; you owe it to your Money. So ask yourself, what can I reasonably expect as a return on my investment and when will I start earning?

Here is my very practical answer. When you deliver the funds, whether by cashier's check or federal funds wire transfer, you have made your investment. That day you begin earning a return. Always remember… sleeping or awake, money costs money. We're investors in a business that costs money every minute of every hour of every day. And… **We can make money every minute of every hour of every day.**

Investment real estate can be a money machine that rewards knowledgeable investors with real, touchable, current and future cash flow and appreciation. Decades of experience have taught my partners and I to look at potential deals with something of a jaundiced eye. Time has shown that our "natural" skepticism, seems to always be justified.

This brings me to the number one (#1) direct Rule, that if not followed while doing your Due Diligence will generally cost more money than any other acquisition mistake… **"Every Seller is a Liar, because Truth is a Difficult Commodity."**

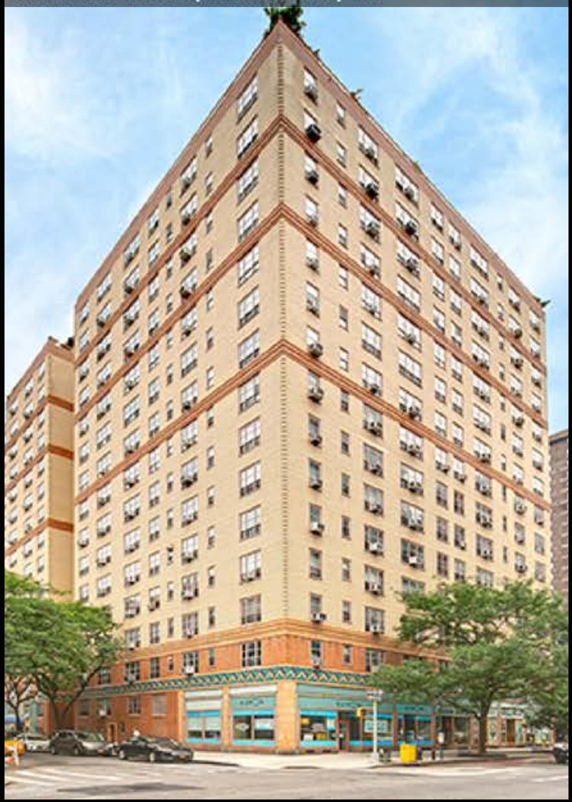
There's no exception to this Rule! Every Seller or his representative will lie in some way shape or form – either by outright misrepresentation, slanting the facts, or simply failing to accurately deliver unfavorable information. In other words, lying by omission. Remember, you owe it to your Money to insist that all the appropriate information is delivered.

A few examples of **"must have"** Due Diligence information:

- Environmental reports for building interiors and if a garden community, random soil tests
- Income statements for three years where ever possible
- Rent rolls for three years where ever possible
- Turnover reports for three years where ever possible
- If the apartment rents are registered because of some type of limit or control as in some cities like New York, an audit of the records of the controlling agency's records
- A copy of the running inventory of the property for at least one year if possible

There are many people who think due diligence is unnecessary. I was told by the senior officer of a national, competing investor, that they receive enough information from the Seller.

GRAMERCY HOUSE, MANHATTAN, NY



Of course, I started to laugh. Your knowledge of the property before closing should be guided by hard, in-depth, independent, confirmed reality…. Facts. **Perception is not Reality!**

Your Perception after listening to a Seller is not Reality. And Your Perception after listening to a Broker is certainly not Reality. So... The Rule always applies... Due Diligence is Mandatory! If you do not complete all the Due Diligence prior to closing the transaction, as soon as you close that same transaction, be sure to go and check yourself into a mental institution. It will probably be safer for you!


TURTLE CREEK, DALLAS, TX

Here are a few other wild and ridiculous statements I have heard over the years from competing investors. *"I'm not worried about current cash flow."* Better yet...*"The improvements we are going to make will overcome any deficiencies, and then we'll sell it for a mint."*

I'm even laughing as I type this article. What kind of absolute fool would buy a property for more than the property's current value? Nobody is wealthy enough to do that. You make your money on the day you buy the property because you're buying the property at its then current value or you're paying less than its then current value. But you never buy a property based on hopes and dreams.

You make your money on the day you buy – never on the day you sell. You collect your money on the day you sell.

For all the investors who want to hold onto their money and make a profit, it's very important to understand that hopes and dreams don't guide this business.More importantly, hopes and dreams do not keep you out of trouble. You must know and understand the pragmatic reality of the moment and the reasonable viability for the future. Like Mark Twain famously said, *"a good way of obscuring reality is to use fancy statistics."*

Take for example an Internal Rate of Return (IRR). Essentially this is a wish a Seller makes when they deliver the **"Property"** information. Specifically, that you may just be uninformed enough to believe the Seller, without Due Diligence.

Be careful. When you buy, be sure to buy what the Seller has to sell, NOT the seller wishes they had to sell.

If you're an investor, be sure that the partners of the Managing Member or General Partner have the pragmatic expertise, and the real life experience to understand the realities, and never get up caught in a Seller's hopes and dreams.

Now, please STOP everything you are doing and focus on these next words. There are Rules, and some minimum standards, to live by when investing in Real Estate. You may bend these rules for other things, for example a larger portion of ice cream, and how much you will pay for a divorce, but you NEVER, ever bend the rules for Real Estate!

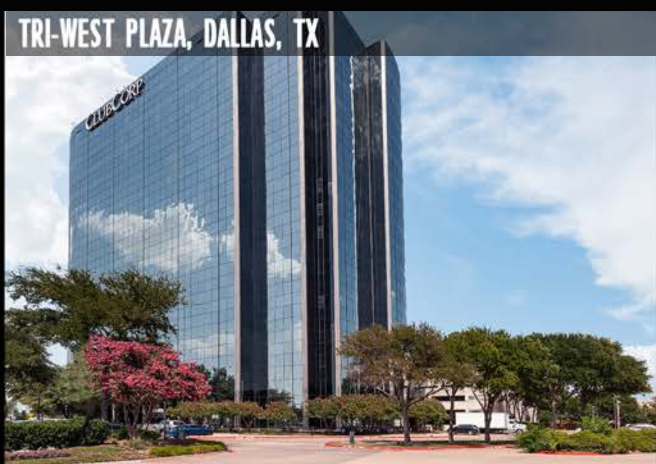
Don't do a partial job when you buy. No one enjoys curing their mistakes because they were too lazy or worse too cheap, when they were doing the Due Diligence work. What about portfolios? Surely the good properties in the portfolio package can carry the one, maybe two laggards, right? That's the way it's been pitched to me many times.

The answer will surprise you, and we'll discuss it together with several other questions in a future article.

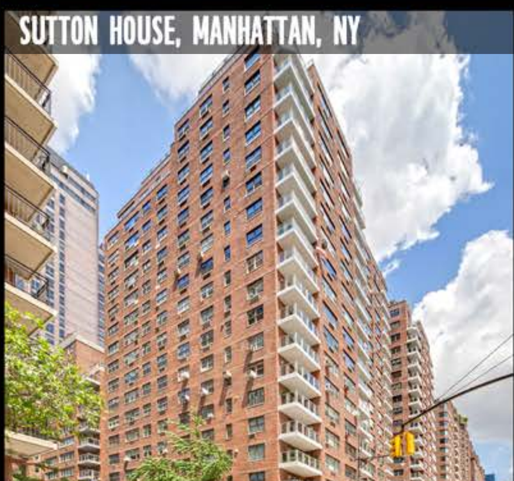
So please, remember that when you are presented with "facts" that have no "basis in fact," it's always best to ask specific questions (nicely and without anger) and push for realistic answers. If you can't get those answers from the seller, go to the Contact page on the Guterman Partners' internet site and click on Ask Gerry a Question.

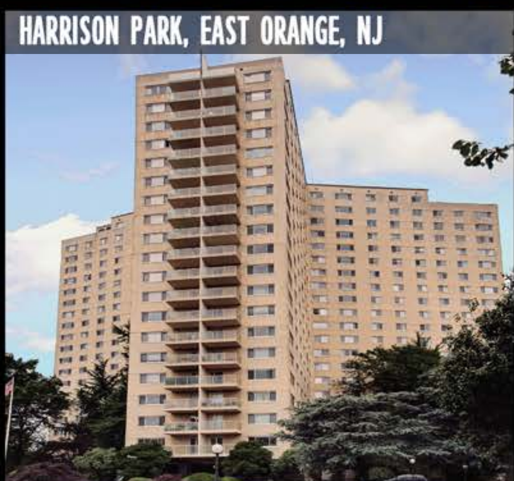
Ask Gerry! There's no charge to you and no expectations from you, period!

A few minutes answering your questions, won't hurt anyone and may be very helpful for you.


TRI-WEST PLAZA, DALLAS, TX


CRYDER POINT, BEECHURST, NY


SUTTON HOUSE, MANHATTAN, NY


HARRISON PARK, EAST ORANGE, NJ


MONTICELLO BUILDING, DALLAS, TX

WHY GUTERMAN PARTNERS? BECAUSE "EXPERIENCE IS EVERYTHING"