

Bargain Sale Case Study

The National Real Estate Foundation's (NREF) staff has been training property managers and real estate agents on the benefits of gifting property. One of the techniques discussed is the "Bargain Sale" concept. It is this approach that helped complete the recent donation described below.

A property management firm, in Albuquerque, New Mexico, was contacted by the owners of a 40-unit apartment complex to establish a management arrangement. The issues facing the owners and the management firm were:

1. 30% vacancy factor
2. Tenants in various governmental subsidies programs weren't compatible with other tenants
3. There was a history of late rental payments and subsequent court action
4. Numerous drug arrests had occurred involving both the tenants and their guests
5. An existing mortgage of \$290,000 was virtually non assumable or owners had to remain as guarantors
6. Owners basis (property acquired via Section #1031 exchange) of \$100,000
7. Location in high crime area
8. The tenants have physically abused property i.e. car destroyed one corner of a building, and unreported water leaks
9. Owners were moving to Mexico to complete a retirement home. The construction project demanded additional funding very quickly or all work would be stopped.
10. Monthly negative cash flow occurred in spite of the owners donating their time to management, repairs, apartment leasing and regular appearances in court on pending eviction litigation.

The professional management firm would not accept the assignment. They did, however, arrange for a meeting between the owners and a representative of NREF. At that meeting the owners agreed to donate their equity over and above the cash necessary to retire the mortgage and provide funds to complete the construction of their Mexico home. The balance of the property's value was to be contributed to NREF. The parties entered into a "Bargain Sale" contract in which NREF agreed to pay donors \$500,000. This would allow the donors to pay off their \$290,000 mortgage and have a \$210,000 cash balance.

During NREF's due diligence period they found a qualified buyer for the complex. It was the buyer and NREF who negotiated the terms of the sale. Both transactions closed simultaneously which allowed NREF to use the third party's money to close on their purchase from the original owners. The donors got released from the mortgage obligation, \$120,000 in cash, a second mortgage for \$90,000 and a charitable gift deduction of \$500,000 based on the appraisal of \$1,000,000.

By identifying properties with low basis, philanthropic owners and their professional advisors can craft creative solutions to apparent problem situations, all parties, therefore, benefit from the outcome.

NREF is willing to explore similar projects around the country and in fact worldwide. Contact us if you have a property you would consider donating all or a part of to our charity.