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## **Learn How Creative Financing Works!**

### **THE MONEY SECTION**

#### **Introduction**

**The first Action Section is the Money Section.**

This is because money is the whole foundation of investing in real estate, even if you are doing a deal using no money at all.

**There are two main topics within the Money Section.**

**They are "Financing Strategies", and "Financing Sources".**

#### **The Purpose Of This Section**

The purpose of this Section is to give you an understanding of how the money side of real estate investing works. For now, we'll mostly be covering the strategies and sources themselves. Then we'll cover how to structure the agreements behind these strategies in the next Section

#### **Understanding Creative Finance Strategies**

First, the key to doing any creative real estate investment deal is to understand the finance strategies that make deals come to life.

We'll break down the money side of real estate investing and look at these strategies from the inside out, forwards and backwards, covering how to do deals using no money, how to structure deals using the existing financing, and how to do deals with new financing. We'll also cover specific strategies for buying a home to live in with no money down, along with strategies that will even allow you to walk away from closing with cash in your hand.

As we go through each of the finance strategies, we'll also help you to identify what type of deals and strategies best fit your abilities and financial goals, so that you can make confident and informed investment decisions.

#### **Knowing The Money Sources**

Most of the strategies in this course do not require you to get any form of new financing. However, there are a few strategies that do. Therefore, you must also understand the sources you can get money from when you need it.

**Some of these money sources include ...**

- \* Banks
- \* Mortgage Brokers
- \* Hard Money Lenders
- \* Partners
- \* Credit Cards
- \* IRA Accounts
- \* And various government loan programs

Even if you never need to get a regular bank loan yourself, there will still be times where you'll need to know how to get your buyers qualified for a loan.

By understanding how banks and mortgage brokers evaluate a loan application, you'll not only know how to get a loan for yourself (if needed), but you'll also be able to more effectively screen potential buyers and ultimately get more properties sold quicker.

It is also important that you understand the more unconventional sources of financing such as hard money lenders, partners, and how to buy real estate using someone's personal IRA account. Again, you must understand these unconventional sources not only for yourself, but so you can help your buyers borrow from these sources as well.

### **Addressing Credit Issues**

Most of the strategies in this instruction also do not require you to have any credit.

However, some situations may require you to get bank financing if the investment route you take requires it.

For that reason, we have included a bonus chapter on repairing your credit if needed.

Even if you already have good credit, you can always work on having stronger credit.

Again, you'll not only want to learn about "credit repair" for yourself, but also so you can help your buyers overcome any credit issues which may prevent them from getting a loan to buy your property.

As we cover the finance strategies, we'll not only cover when you do and don't need money, but also when you do and don't need credit. This will help you decide which investment strategies are best fitted for your money and credit situation. It will also help you to identify any shortcomings or road blocks you'll have to overcome for you to be able to do a certain type of investment.

### **The Truth About No Money Down**

Before we get started, let's talk for a few minutes on the truth about buying real estate with no money down and some of the misconceptions many people have. You may have preconceived ideas as to how no down payment real estate investing is actually done, but chances are many of your perceptions are wrong.

There are numerous ways you can buy real estate with no down payment. Some of these ways include getting seller financing, doing a lease option, buying a property using private money, or flipping a property wholesale.

### **Can The Seller Still Get Cash?**

One misconception many people have is that "no money down" means the seller does not get any money, but this is not always the case. It just means that you as an investor are not going to take money out of your pocket to buy the property. Many times the seller will get money and this money could come from any number of sources. The money could come from a loan you borrow, or the money could come from your end buyer (if you are doing a wholesale flip). In a case where the seller holds a seller held mortgage, you could help the seller sell some of the payments on the note to a note buyer.

### **O.P.M. - "Other People's Money"**

As the old saying goes, "it takes money to make money". However, the money it takes does not have to be your own. It can be OPM (other people's money), or even other people's credit.

Just for starters, the OPM you use could be money from a private lender or partner, and even could be the seller's existing financing. There are numerous ways you can make money in real estate without taking money out of your own pocket or using your credit. By the way, if you want to become truly wealthy in real estate, you must learn how to use other people's money to do it.

So, it doesn't take your own money to make money, it just takes the knowledge of how to make money either without using money, or by using other people's money. That's what we're going to cover right now.

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## **Introduction To Creative Financing Strategies**

Every real estate deal requires some form of creative financing technique. To understand these techniques better, we're going to **break them down into three main categories.**

### **1. No Financing**

The first category is "No Financing". That's right. You can do deals that require no financing at all, such as when you buy a property and immediately sell it to another buyer. This is the "flipping" technique we spoke about in the first Section.

## **2. Existing Financing**

The second category is "Existing Financing". This is where you structure the deal around the seller's existing financing. What usually comes to mind is an Contract For Deed or a Lease Option.

## **3. New Financing**

The third category is "New Financing". This is where the deal requires you to get some form of new financing, either from a bank or a hard money lender. Usually, the only time you'll need to get new financing is when you're going to buy a property, fix it up and retail it, or when you're going keep a property as a long term rental.

Realize though, buying a rental property does not always require you to get new financing. Many times, Landlording (and even retail deals) can be structured around the seller's existing financing, but there will always be some deals that require you to get new financing.

Let's cover each of these three categories so you better understand when you need money and/or credit, and when you don't.

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# **1. Investment Strategies Requiring "No Financing"**

The first category is the investment techniques that don't require any financing.

No Financing = No Qualifying & No Money

Of course if there is no financing involved, it means you don't need any credit because there isn't any financing for you to qualify for. It also means that you don't need any money. What little money you might need would usually be for binder deposits. So this category is especially important if you have limited funds and/or bad credit.

## **Flipping Real Estate**

The most popular way to make money in real estate using no money, credit or financing, is by "flipping" property. This is where you put a contract on a house and then either assign the contract, or do a double closing. Again, you most likely will have to put a binder deposit down on the deal with the seller, but you can quickly get this money back by getting a new binder deposit from your new buyer.

Using this strategy, you will get the property sold before you even have to close with the seller. By having a contract to buy the property, you have what is called an "equitable interest". This means you can sell your right to purchase the property to another buyer by assigning the contract for a fee. You can also give your buyer a new purchase contract saying you will sell the property to them right after you buy it from your seller. This is the double closing we just referred to.

## **A Double Closing**

The key to flipping is the double closing which is also commonly referred to as a "double escrow", "simultaneous escrow" or "simultaneous closing".

What you do to flip a property is schedule your closing with the seller, and then schedule your closing with your new buyer to be done right afterwards. You'll take title of the property just long enough to immediately resell to your buyer.

At closing the buyer will bring the funds to purchase the property either in cash or by getting a loan. The closing agent will take the money from your buyer and use it towards your purchase closing with the seller. Both closings are done back-to-back and the cash flows from your buyer to your seller simultaneously. This is why this type of closing is commonly referred to as a "simultaneous closing".

In the end, the closing agent subtracts how much you bought the property for from how much you sold it for and you will walk out with a check for the difference. We'll cover double closings in more detail in the next Section on agreements.

## **Buyers Lists**

To flip a property effectively, you should have a list of potential buyers ahead of time. By having buyers already lined up, you'll be able to more effectively target your buying efforts and be able to make offers with more confidence knowing you can get the property resold before you have to close with the seller.

### **Have A Backup Exit Strategy**

Of course, you should always have a backup strategy incase you are not able to get the property resold fast enough. After all, you signed an agreement saying you would purchase the property. If you failed to do so, not only would you lose your deposit, but possibly your reputation.

A knowledgeable investor will have a backup plan in place ahead of time just incase they can't flip the property in time. What most investors do is get a private loan to purchase the property until they can find a new buyer. At that time, the new buyer either assumes the private loan or the private loan gets paid off. Don't forget, you only need hard money as a back up for when you do not sell the property before you have to close. We'll cover more about the sources of these types of loans later in this Section.

There is another way you can flip a property without having to worry about not being able to close and that is by simply "optioning" the property.

When you option a property, you are not saying you definitely WILL purchase the property. In fact, you'll be letting the seller know upfront that you only plan to exercise your option once you find another buyer. Also, not only do you still not need any credit, but you can get into the deal using a smaller deposit, and how you close the deal is the same as if you had a regular purchase agreement on the property. You can either assign the option for a fee or do a double closing.

### **Using A Standard or Straight Option**

This technique is usually only used when dealing with home owners or private investors, and almost never used when trying to buy property from a bank.

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## **2. Structuring Deals Around The "Existing Financing"**

The second category of investment techniques are those that are structured around the seller's existing financing. With these techniques, you'll be showing the seller how you can solve their problems and give them debt relief by either taking over their loan or structuring an agreement that allows you to make their payment for them. This does not mean you will be formally assuming loans from sellers.

### **No Qualifying To Assume Loans**

As a real estate investor, it is not necessary for you to formally qualify to assume loans. Besides, many mortgages are not formally assumable and the credit criteria required to assume a loan is the same as when you get a new loan. Also, you don't need to put your personal credit on the line to do deals.

### **Buying "Subject To"**

One way to structure a deal around the existing financing is to take over the property "Subject To" the existing loan. In case you have forgotten, this means the seller is willing to deed you their house if you agree to make the payments on their loan.

There are many sellers out there who are facing foreclosure and are willing to deed you their house if you will save them from being foreclosed on. This way, the seller's credit is saved, which may mean a lot to them. In other cases, the seller may not care about their credit, but they'll still deed you the house if you're willing to give them some moving money.

### **No Credit Required**

When you take a property "Subject To" the mortgage, you are not formally assuming the loan; therefore, you won't be using your credit to do the deal. Also, your name does not appear on any of the bank's documents and you're not personally liable to the bank for payments on a note you took over "Subject To".

### **Little Or No Money Required**

The only money you will need would be for making up any past due payments the seller didn't make. You may also agree to give the seller some moving money as part of the deal. From then on, the only other money you should need would be for any repairs and of course the monthly payments on the seller's loan.

### **Very Little Closing Costs**

The only closing costs you will have are for recording the deed. We'll cover how to draw up your own quit claim deed in the Agreements Section and there is no need to have a formal closing at a title company. You can simply have the deed notarized and then go down to your court house and have it recorded. In addition to paying a recording fee on the deed, some states may require you to pay a transfer tax.

When taking over a property, it would be in your best interest to at least have the title checked, which could cost you a couple hundred dollars. You can get title insurance on a property you took "Subject To", but you may find a few title companies that won't write you a title policy. Usually, a title company will make an exclusion in the policy stating the property's title does still have a mortgage against it.

Realize, just because a seller transfers title does not mean the loan goes away. The loan remains as a lien against the property in the seller's name until that lien is paid off or assumed. Until then, you'll be making the payments on behalf of the seller.

### **Claiming The Tax Benefits**

The interest on the payments you make are even tax deductible and you don't need the interest statement from the lender to be able to claim it on your tax return. Just because the tax statement the lender sends to the IRS is in the old owner's name, does not mean you can't claim it on your own tax return. If you get audited, all you have to do is produce copies of the checks where you were the one who paid the interest.

### **Making The Mortgage Payments**

To make the payments, the only thing you're going to do is mail in your check to the lender. You don't have to ask their permission to send them money on behalf of the seller. If you send them money for a payment, they will take it. .. no questions asked.

When the bank receives the payment, they send it to their data entry department which enters the loan number you wrote on the check, and the dollar amount paid, into their database. The person doing this data entry goes from one check to the next, one right after the other. When entering each payment, they don't look up the account by the name; they look it up by the loan number.

By the way, do not try to change the name on the coupon book or the address the coupon book is sent to. It doesn't matter whose name is on the coupon and the new . books should be coming to the property's address anyway. If you don't have the coupon book, don't worry about that either. Just mail in the payment without it and don't forget to put the loan number on your check.

You never want to personally confront the bank and tell them that you are taking over payments on the loan without formally assuming it. Also, don't try to create problems by asking the bank to change anything in regards to the mortgage and whose name it is in. Just make the payments.

### **Circumventing The Due-On-Sale Clause**

If you're still worried about the due-on-sale clause, there are ways to try and circumvent it, or at least hide the fact you took over the property from the seller.

### **The Garn-St. Germain Act**

The most popular way investors get around the due-on-sale clause is by using the **Garn-St. Germain Depository Institutions Act Of 1982**. This act outlines certain cases in which a lender may not exercise their right to call a loan due under the due-on-sale clause.

See our downloadable copy - [Garn-St-Germain-Depository-Institutions-Act.pdf](#)

Under this federal law, it says that a lender can not call a loan due if the seller puts their property into a land trust for estate planning purposes. Furthermore, the Garn St. Germain Act does not just apply to owner occupied properties. The law simply says it applies to single-family residences, and because it is a federal law, it applies to all fifty states.

The specific paragraph we are referring to is **paragraph D8** of the file, which reads as follows ...

***"A transfer into an inter vivos trust in which the borrower is and remains a beneficiary and which does not relate to a transfer of rights of occupancy in the property. "***

When necessary, **some investors have the seller put their property into a land trust with the seller as the beneficiary. This is covered under the Garn-St. Germain act because it is a transfer into an inter vivos trust and the transaction does not relate to the rights to occupancy in the property.**

- The seller then assigns their interest in the trust to the investor.
- This does give rise to the due-on-sale clause; however, this is done on a separate document that is not required by law to be recorded.
- Furthermore, usually the only people who have a copy of the transfer document, are the seller and the investor.
- If the lender sees there was a transfer into a trust, they may ask for a copy of the trust for their files, usually by sending you a letter.

- If the lender does ask, simply ignore the letter and see if they send you a second one. If the lender still wants to push the issue, you simply mail them a copy of the land trust showing the original owner as the beneficiary in compliance with the Garn-St. Germain Act.
- Of course, you'll want to conveniently forget to include a copy of the assignment of beneficial interest.
- We'll cover more about land trust agreements and all the documents involved in detail, later in the Agreements Section.

### **Will Lenders Call A Loan Due?**

Most banks won't cause you a problem even if they did somehow realize you took over the property. Banks already have enough problems with loans that are in default. They don't want to create more defaulted loans by calling loans due which are paid up to date. Banks would rather have the money than have the house because the house becomes a liability on their books and even affects how much money the government will allow them to lend out on new loans.

This is not to say banks never exercise the due-on-sale clause, but it is extremely rare.

### **If The Seller Has An Equity Line Of Credit**

One circumstance in which a lender will call the loan due almost 100% of the time, is when the seller has an open equity line of credit on the property.

This is because the seller could go down and borrow money against the property, which they no longer own. So, if the seller has a credit line on the property, do not purchase it until that credit line is closed. You can find out if a seller has a credit line simply by asking them. Just in case the seller doesn't tell the truth, any open credit lines will still show up in a title search.

### **What If A Bank Tries To Call The Loan Due?**

There is always the slim chance the lender will call the loan due, or at least pressure you to qualify to assume the loan, if they figure out you took over the property "Subject To".

If the bank tries to call the loan due or tells you that you have to pay it off or qualify to assume the loan, you can tell them you are not going to do it. You can even point out that you have not signed any paperwork which says you will pay off the loan or qualify to assume it. If you bailed the original owner out of foreclosure, you'll also want to point out to the bank that at the time you took over the property, the original borrower was several months behind.

To help discourage the bank, you can further tell them the property is in poor condition and if they call the loan due, you will abandon the property. Also, you cannot guarantee what the condition of the property will be in when the bank gets it back, because the neighborhood is subject to random vandalism.

Furthermore, you can let the lender know you will continue to mail in the payments and they can either cash the checks, or take the house back. That is ... Whatever house may be left by the time they get it back.

The bank may think you're implying you'll do something to the property, but that is fine. Of course, you're not really going to vandalize the property, but the statement is true. If the lender is going to call the loan due, you're not going to continue maintaining and watching over a property you will no longer own. You also can not truly guarantee the property will not be vandalized. The bank can draw their own conclusion about the statement. If they're going to play hard ball ... play hard ball back! Some banks may be just too stupid to realize you are doing them a favor by making the seller's payment for them.

By the way, if the bank calls the loan due and actually files for foreclosure (which rarely happens), the foreclosure will not show on your credit because you never signed on the note as a borrower. Also, the most money you can lose is whatever you have invested.

This should not be very much if you got a good deal.

**If you are not willing to risk that, then this technique may not be for you and you may want to look more heavily at the Lease Option method.**

It may be to your psychological benefit to go to your local investor association and talk with some real estate investors who have taken over houses "Subject To" mortgages that had due-on-sale clauses. Most, if not all of them, will probably tell you they never had any problem.

## **Wrap Around Mortgages**

Another way to buy a property structured around the existing financing, is a "wrap around mortgage".

In this scenario, the seller is also willing to deed you the house and is not worried about the due-on-sale clause. Realize, **we are not talking about a second mortgage for the remaining balance of the sale** after you subtract the first mortgage from the sales price.

## **We are talking about a mortgage for the entire sales price.**

To make this more clear, let's give an example ...

- Let's say you're buying a house for \$100,000, with no money down, and the seller owes \$80,000 to a bank.
- You would give the seller a wrap around mortgage for \$100,000.
- You would make the payments on your \$100,000 loan to the seller and the seller would make their payments on the underlying \$80,000 to their bank.
- See, the \$100,000 mortgage you give the seller "wraps around" the seller's existing \$80,000 loan.
- This is also commonly referred to as an "all inclusive mortgage" or an "all inclusive trust deed".

It is different from a seller carry second mortgage in which you would give the seller a \$20,000 mortgage, and then make payments to the seller for the \$20,000 while making a separate payment to the bank for the \$80,000.

## **Contract For Deed**

The next technique we're going to discuss, which can be structured around the seller's existing financing, is a Contract For Deed. This is also commonly referred to as a "**land contract**" or an "**installment sales contract**".

Under a Contract For Deed, the buyer agrees to make installment payments on the property but they do not get a deed to the property. The seller agrees that once the buyer has paid for the property, they will deliver a deed to the buyer. This is basically the same as seller financing or a mortgage, except for the fact that the buyer does not receive title until later.

The seller could also agree to convert the Contract For Deed into a mortgage after a certain number of installment payments have been made, but before the entire purchase price has been paid. This gives the seller a chance to test-drive the buyer before transferring title and giving them a mortgage.

### **No Credit Required**

Again, because this is a form of seller financing, you don't need any credit unless the seller specifically asks to see your credit report.

### **Little Or No Money Required**

The only money you will need is what ever the seller requires down.

### **Closing Costs**

Your upfront closing costs will be minimal because most of them come later when you fulfill the terms of the agreement and the seller transfers title. Even then, your portion of the closing costs can many times be rolled into your loan, which means they won't have to come out of your pocket.

Some states do require a Contract For Deed to be recorded for the agreement to be valid. If this is the case in your state, you'll have to pay a few bucks upfront to record the agreement. Even if your state doesn't require it to be recorded to be valid, you'll still want to record it just so you know your interests are secured against the property. You also should pay to have a quick title search done to make sure the title to the property you are buying is clear.

## **Lease Options**

The most popular way to buy real estate by structuring the deal around the seller's existing financing is by doing a Lease Option. This is because Lease Options have so many benefits for both the buyer and the seller.

### **Little Or No Money Required**

First, you can take control of a property using very little or even no money. Most of the time, any money you put down would be about the same as a security deposit on a regular rental lease. This is assuming you are not bailing the seller out of a foreclosure in which they are several months behind on their mortgage.

### **No Credit Required**

Again, because this is a form of seller financing, you don't need any credit unless the seller specifically asks to see your credit report.

### **Closing Costs**

Another great thing about Lease Options is that there are no upfront closing costs. This is mainly due to the fact the closing does not take place until you exercise your option to buy. Just like with an Contract For Deed, you can sometimes refinance the agreement and roll your closing costs into the loan. If you happen to be sublease optioning the property, what ever closing costs your seller does not pay, can be passed onto your tenant/buyer.

## **Lease Option VS. Lease Purchase**

There are some very distinctive differences between Lease Options and other financing techniques you should understand.

## First, is the difference between a **"Lease Option"** and a **"Lease Purchase"**.

Very simply, a Lease Option says you have an **"option" to buy the property**, and a Lease Purchase says **you are "purchasing" the property**.

- The main difference is that with a Lease Option, you do not have to buy the property if you decide not to exercise your option.
- Under a Lease Purchase arrangement, you are agreeing right from the start that you are purchasing the property.
- This means that a Lease Purchase is almost identical to a Contract For Deed because it is an installment sale.
- On the other hand, a Lease Option is very different from an Contract For Deed.

### Lease Option vs. A Contract For Deed

As we just stated, a Lease Option gives you the "option" to buy.

- This option does not state that you are buying or must buy.
- It simply states you have the option of buying, if and when you are ready.

A **Contract For Deed** says that you as the buyer "are "buying" and will get title to the property after you meet the terms of the agreement. **Thus, an Contract For Deed is an installment sale.**

**Many people argue that a Lease Option agreement is also an installment sale if the tenant/buyer is getting a monthly rent credit towards the purchase price of the house.**

- The main difference is that under a Lease Option arrangement, the rent credits only apply after the tenant/buyer exercises their option.
- Also, the tenant/buyer only has an option to buy.
- Until this option is exercised, there is technically no active agreement for sale.

Also, **the seller under a Lease Option does not have to file foreclosure** like they would if they sold under a Contract For Deed. This is especially important if you plan to be the seller.

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## 3. Investments That Require "New Financing"

The last set of investment techniques are those which require you (as the investor or homebuyer) to get "new financing". By the term "new financing", we are talking about financing which does not have anything to do with being structured around the seller's existing financing.

Some of these new financing sources include bank loans, loans from hard money lenders, partners, and even borrowing money from some one's IRA account. We'll be covering more about these sources later in this Section. But first, let's take a look at when you may need new financing.

### When Do You Need New Financing?

As we discussed in the first Section on getting started, the types of investments you can do are broken down into four Deal Sections.

Those Deal Sections are

- "Wholesaling",
- "Retailing",
- "Seller Financing", and "Landlording".

**Now, in the Wholesaling Section, you won't need any new financing because you'll be flipping the deal to your new buyer by either assigning the sales agreement for a fee, or by doing a double closing.**

- The only time you might need new financing in this Section is only as a backup for if you happened to not get the deal flipped before you had to go to closing with the seller.
- So in essence, the Wholesaling Section does not require new financing.

In the **Seller Financing Section**, the deal is structure around the seller's existing financing.

- This means you won't be going to any outside sources for new financing.



That only leaves the **Retailing Section** and the **Landlording Section**, as the types of investments which may require you to get new financing.

Let's take a look at each of these two Sections.

## Retailing Section

In the Retailing Section, **you will almost always need new financing to purchase and repair the property.**

- You can sometimes control the deal using some form of seller financing.
- However, many of the best deals for retailing usually are bank owned properties and to get the best price, you'll be offering the bank all cash.
- Even if you were to get some form of seller financing, you'll still need to come up with the money to do the repairs. After all, you have to buy the property well below market so you have a profit margin and this almost always means the property needs work.
- So, unless you can get seller financing and you have the money in your pocket to do any necessary repairs, you're going to need some type of new financing.

### Bank Loans

Your first thought might be to try and borrow the money from a regular bank. However, most banks don't lend on a property that needs repair work. These repairs are what lenders commonly refer to as "deferred maintenance", because the repairs needed are from maintenance which has been deferred.

Banks also rarely ever lend money for repairs. They especially don't like to lend more money than what you are buying the property for. On top of that, banks tend to look for you to put money down. The final blow is banks want you to have good credit and a good job history.

**The only thing banks are good for when it comes to Retailing is getting loans for your buyers.**

### Government Loan Programs

You might be thinking ... Well what about those government loan programs where the government gives you a low interest rate and even loans you money to do the repairs?

There are numerous government programs out there for buying and repairing residential houses. There are even special programs for historical homes.

**But the most popular program people are referring to is the 203K loan.**

- With this type of loan, you can buy a property and get money for doing repairs at a great interest rate. However, the red tape is enormous!
- These types of loans almost always require credit qualification.
- You'll also need written estimates from several licensed contractors.
- Finally, once you do get the loan and start doing repairs, getting money out of the escrow account is like pulling teeth.
- For these reasons, we won't be covering these types of loan programs in great detail.
- There are just too many other ways to get your hands on the money you need without having to jump through hoops or bang your head against a brick wall.

## Hard Money Loans

One of the best ways to get the new financing you need to do a retail deal is directly through a hard money lender or a mortgage broker who specializes in hard money loans.

- With these types of loans the interest rate can range anywhere from 12 to 18 percent.
- This may sound high at first, but usually the payments are "interest only", so the payment technically is not high at all.
- Besides, it is well worth it to pay a few extra bucks not to have to deal with the red tape of a bank or government loan program.
- Some lenders (or brokers) do require you to have some kind of credit, but many do not. The best part is, not only do these lenders routinely loan out 100% of the purchase price, but most will even lend you the repair money necessary if there is enough equity.

## Private Loans

- You can also get loans through private individuals directly. These are still considered to be hard money loans.
- The only difference is you won't have to pay a broker fee.
- You also get to deal one-on-one with the person who has the money and if the deal is right, you may even decide to bring the lender on as a partner in your deal.

## Using Someone's IRA Account

Another great source of financing is by using the funds in an IRA account.

- This could either be your own account or you could show other people how they can be your private lender by investing the money in their account.
  - Many people who have IRA accounts don't realize they can invest in real estate by "self directing" their funds. We'll talk more about this and the other types of financing sources, later in this Section and in the Contacts Section.
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## Landlording Section

The other time you may need new financing is in the Landlording Section.

When buying rental properties you many times can structure the deal around the seller's existing financing. If you can't, you'll obviously need some form of new financing to be able to buy the property. Even if you do get the seller to work with you short term, you'll still need new financing later if you plan to keep the property for yourself.

So, if you plan to own a rental property long-term as a source of cash flow, you must be able to work your way into having long term financing and there are several scenarios in which you could do this. Let's look at each scenario individually ...

### Scenario #1 - Long Term Seller Financing

The first scenario is to get the seller to give you some form of long-term seller financing. This could either be by deeding you the property "Subject To", or by doing a long-term Agreement For Deed or Lease Option.

In this scenario, the entire deal rests on the seller's existing financing and doesn't require you to get a loan from any outside source, either now or in the future.

### Scenario #2 - Short Term Seller Financing, Then Refinance

The second scenario is to get the seller to at least work with you short-term and then get a new purchase loan, or refinance loan, later. This could be done by getting the seller to do a short term Lease Option with a term of at least one to two years, or by getting the seller to do a short-term balloon mortgage. With a balloon mortgage, the seller would finance the property short-term and then the balance of the mortgage would balloon and be due after two to five years.

In either case, you would later get new financing from an outside source, usually at a bank.

### Scenario #3 - Short Term Alternative Financing, Then Refinance

The third scenario is to get into the deal using private funds or a hard money loan. But, these loans tend to have short terms of one to two years, and the interest rates tend to be higher than normal.

The key to this strategy is to get into the property, get it fixed up and rented out, and then refinance the high interest rate hard money loan with a lower interest rate bank loan. This is the most popular strategy used by investors when buying run down properties they plan to keep as part of their rental portfolio, and there are several reasons why.

First, it is easier to get a refinance loan from a bank on a rental than to get a purchase loan, because the credit criteria is more lenient. This is mainly due to the fact you have a past payment record on the loan you are refinancing.

Also, if you get a regular purchase loan from a bank, the bank will usually look for you to put money down. To avoid this, it is better to buy a property using private hard money and then refinance the property after six to twelve months. This is because you can get a hard money loan without putting any money down. It is also easier to borrow extra money for repairs when getting a hard money loan.

Later when you refinance with a regular bank loan, instead of putting money down, you can even get money back at closing by borrowing more than what is owed on your underlying hard money loan. That's right, not only can you get money back when you initially buy the property using a hard money loan, but you can also get money back when you refinance with a bank!

### Scenario #4 - Get A Non-Owner Occupied Purchase Loan

The final scenario is to get a regular purchase loan from a bank. But as we just stated, most banks require you to put money down and because you are applying for a nonowner occupied loan, they may require as much as 30% down!

Another issue with getting a non-owner occupied purchase loan is that the property will usually have to be in good condition and already be rented out. This can be a problem if you are buying a run down vacant property.

The credit qualifications for a purchase loan are also more strict than if you were applying for a refinance loan. Therefore, the second or third scenarios may be the best route for you to go if you have limited credit.

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# Determining Which Finance Strategy To Use

We have covered the ways to buy real estate using "no financing", the strategies you can use to structure deals around the "existing financing", and what types of investment strategies require you to get "new financing".

**The question now is ... How do you know which investment technique you should use and which Deal Section the deal best fits into?**

## Factors That Determine The Deal Section & Finance Strategy

There are five main factors which will determine what financing techniques you should use and what you should do with the property. They are the seller's needs, any existing financing, the property's condition, your financial abilities, and of course ... your investment goals.

Let's look at each of these determining factors one-by-one:

### 1. The Sellers Needs

First is the seller's needs. In every real estate transaction you should seek a solution which is profitable to you, yet gives the seller what they need out of the deal.

If your offer does not fulfill the needs of the seller, chances are they won't accept it. For example, if the seller is a private owner facing foreclosure, the seller may simply need for someone to take over the loan and help save their credit. But, the seller may be reluctant to do the deal if they need some moving money and your offer does not give it to them.

So, talk to the seller and find out why they are selling their home and what they truly need out of the deal, then make sure to structure your offer to solve their problems and needs.

### 2. Any Existing Financing

The second determining factor on what finance strategy to use is the existing financing.

In the case of a **private owner facing foreclosure**, you may be able to take over the existing financing and create a Win-Win situation that also solves the seller's needs as we just discussed.

However, in the case of a **Bank owned property (REO)**, there is no longer any existing financing; therefore the Bank would be looking for you to pay cash.

### 3. The Property's Condition And Location

The next thing to consider is the property's condition and location.

- For instance, if the property is in a run down area, **it probably won't be the best candidate for retailing.**
- In contrast, if the property is in an upscale neighborhood and in excellent condition, it probably won't be best suited as a rental.
- Also, if you plan to flip the property, is the property in the area your investor-buyers are looking for and does the property need more work than most investors are willing to do?
- If you're looking to own the property as a rental, is it in the area you are looking for?
- The same holds true about looking for a home for yourself to live in.
  
- **It may seem like the property's condition and location are simple factors to consider, but these are major determining factors as to what Deal Section the property best fits into and what finance strategies you will have to use.**

### 4. Your Financial Abilities

The fourth factor we're going to talk about is your financial abilities.

- What might instantly come to mind is your credit or the amount of money you have. This is not necessarily what we are talking about.
- Yes, some deals might require you to have a little money, and some deals might require you to qualify for a loan.
- But what we're mainly talking about is your ability to either do the deal without needing money or credit, your ability to structure the deal around the existing financing, or your ability to borrow the necessary financing without needing money or credit.

The key is to gain the knowledge on how to do deals without needing money or credit, by studying the techniques in this instruction.

Remember, knowledge is a very powerful force, but you have to put it to action!

Therefore, you have to go out and build up your financing sources which don't require money or credit.

We'll be covering more about the sources of financing later in this Section and we'll also be discussing how to build a team of financial contacts in the Section on the Contacts Section.

**Just remember ... The ability to structure any investment without needing money or credit is a financial ability in-and-of itself.**

## 5. Your Personal Investment Goals

The last factor for determining which Deal Section a property fits into and what finance strategy to use, is your personal investment goals.

### Are your goals

- to flip a few properties and make some quick cash, or
- are you looking to build a portfolio of Landlording?
- Are you looking to do a retail deal, or maybe you want to create some no-qualify seller financing for yourself on a home to live in?

This is what we referred to in the Planning Section as ... **"knowing your exit strategy"**.

You must know going into the deal what you plan to do with the property and the property should fit the exit strategy you are planning.

In other words, if your goal is to build a rental portfolio, the property should be suited for being a rental.

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## Creative Home Buying Strategies

If you are looking to buy a home for yourself to live in, there are certain finance techniques you're going to focus on.

### Getting Creative

Of course, if you have good credit and money to put down, you can probably get a regular bank loan without too much trouble. However, not everyone has the best credit possible or the money saved up for a large down payment. This is not to say you can't buy a home though; all it means is you have to be a little creative.

One of the keys to buying a home for yourself to live in without needing money or credit is to structure your purchase around the seller's existing financing. By now, you should have a basic understanding of how this is done from the techniques we have already covered. Mainly, there are four techniques you'll want to consider when buying a home using no money or credit. ..

### Buying "Subject To"

The first technique is to take over the seller's property "Subject To" the existing loan.

- This requires absolutely no credit and the only money you might need would be for any past due payments to bring the loan current, and any moving money you agree to give the seller.
- The only issue to really consider when using the "Subject To" technique to buy a home is the due-on-sale clause.
- If the due-on-sale clause is a concern for you, you can consider one of the other techniques.

### Seller Carry Equity Mortgage

You can sometimes get the seller to hold seller financing. There are some sellers out there who own their property free-and-clear.

- However, the majority of the sellers will still owe a mortgage. In this case, you could still structure a wrap around mortgage or consider one of the next two techniques.

With **Seller Carry Mortgages**, some sellers may want to take a look at your credit and most will want some kind of down payment.

- You'll also be looking at having to pay some upfront closing costs.
- For these reasons, getting a seller held mortgage is not the most popular way to buy a home using no money or credit, but it is still done.

## Contract For Deed

The Contract For Deed technique is a more popular way to get yourself into a home. Again, you usually won't need any credit unless the seller asks to see your credit report and the money required down can be very minimal. The upfront closing costs are still very minimal as well.

Even though a Contract For Deed does still give rise to most due-an-sale clauses, most sellers and buyers feel comfortable that the bank will not give them a problem seeing as how the title has not yet transferred.

## Lease Options

Finally, the most popular way to buy a home using little or no money and no credit, is by doing a Lease Option.

- This is the easiest technique to get a seller to say "yes" to, because everyone is familiar with the term "rent to own".
- Also, the Lease Option technique does not give rise to the due-an-sale clause which may be a concern for some sellers.

Just like with a Contract For Deed, **you may not get title to the property right away, but you do control the title to the property and you are living in it.**

- In addition, most mortgage lenders consider both a Contract For Deed and a Lease Option to be an installment sale, which means you can refinance your way into having title in your own name.
- Best of all, with both a Lease Option and an Contract For Deed, part of your monthly payment is going towards how much you owe.

## Flexible Bank Loans

There are also flexible bank loan programs which you may qualify for as a homebuyer, even if you have a limited credit or very little money to put down.

### First Time Home Buyer Loans

First, there are a lot of "first time homebuyer" loan programs for which you may qualify, if you have never bought a home before. Some programs even consider you to be a first time homebuyer if you haven't owned a home in the last 5 years or so. Under these programs, the credit criteria is much more lenient than when qualifying for a regular purchase loan and **many programs only require 3% down.**

### Low Doc Loans

If you are self-employed or are unable to prove your income, there are loan programs which require less documentation to qualify for.

- These are called "low doc" loans.
- For instance, if your credit is strong enough you could state how much you make and the lender will not require you to document the dollar figure.
- This is commonly referred to as a "stated income" loan.
- The interest rates may be higher on these types of loans, but you can always refinance later for a lower rate, after you have established more credit or income.

### Government Programs

If you are in the moderate to low income bracket, you may qualify for a first-time homebuyer program in which the government will loan you your down payment.

- The different programs usually have minor hoops you have to jump through, such as taking a class, going to credit counseling, and drawing up a household budget.
- Many of these programs have maximum income guidelines where you cannot make over a certain amount of money per year for the household at the time you get the loan.
- However, these guidelines are usually fairly lenient and you would be surprised that you don't have to be poor at all to qualify for the government programs.

### Local City And State Programs

There are also local city and state programs for which you may qualify for as well.

- For instance, most cities have what is called a "bond program".
- This is where the city is allocated a certain amount of money each year to give out as down payment assistance.
- Some of these grants don't have to be paid back unless you sell your home and some may never have to be paid back at all.
- If you are a first-time homebuyer and are looking to purchase your home with no down payment, you must check into these government programs.
- We'll be covering more about finding these finance sources later in this Section.

## Get Pre-qualified

The only way to find out if you'll qualify for any of these programs is to meet with a mortgage broker and make an application.

- The worst that could happen is you would get denied, but at least you would know where you stand.
  - You may also learn that you don't qualify right now, but if you work on your credit (as we'll be discussing in the bonus chapter of this Section), you may be able to qualify later.
  - Until then, you can work on buying a home using some of the more creative techniques we talked about earlier.
- 

## The "Short Sale" Strategy

One creative investment technique we haven't covered yet is how to do a "Short Sale".

**A short sale is simply getting a lender to take less than what is owed on the loan.**

The term "short sale" comes from the fact that the seller will be selling you their property for a price which leaves them "short" of the money to payoff their loan.

For example, if a seller owes the lender \$50,000 on their property, and the seller sells the property to you for \$40,000, the seller is going to be roughly \$10,000 short of money to payoff the lender.

Thus the term "short sale".

## When & Why Lenders Will Do A Short Sale

Most of the time, a lender will consider giving a discounted "short sale" payoff when the seller is behind on their mortgage and the loan amount is at (or near) the property's market value. Sometimes, lenders will even discount the loan payoff when the loan amount is well below the market value, especially if the property is in poor condition.

Some people believe that banks like to foreclose on property because they can take a property back for less than it is worth. Nothing could be further from the truth. Earlier we talked about lenders not wanting to enforce the due-on-sale clause when you take over a property "subject to", because if they foreclose on a property, it affects how much money the government will allow them to lend out on new loans. Also, there are other side effects such as lower company stock prices, and the possibility the bank could lose money when getting the property marketed and resold. The same holds true about getting a lender to do a short sale. If the lender can take a discounted payoff now, it saves them from the costs of foreclosure and all the other problems that come with taking back the property.

## VA And FHA Insured Loans

Even if the loan is VA or FHA insured, it still is not in the lender's best interest to take back the property. It is especially not in the lender's best interest to file a claim with the FHA or VA if the money they will get back is minimal, because FHA and VA do not insure the entire loan.

## When Will Lenders Not Do A Short Sale?

Not all lenders do short sales. Some are simply stubborn and don't know how to save their losses. However, most banks do short sales on a regular basis, but even those banks have instances in which they won't discount the loan payoff.

The most common instance in which a lender won't discount is if the seller is not behind on their payments, because lenders just aren't going to take a discount on a loan that is being paid.

Don't expect a low loan-to-value first mortgage to take a discount if the property is in excellent condition. A low loan-to-value first mortgage holder will usually only take a discount if the property needs extensive repairs and the seller is filing bankruptcy, which by the way will hold up the foreclosure process.

## Can I Do A Short Sale With No Money Or Credit?

Doing a short sale requires no money or credit when it comes to getting the lender to take a discounted payoff. You will however have to come up with the money to pay off the seller's loan.

Remember, with the short sale strategy, you're not negotiating to take over the debt. Instead, you're negotiating a discounted pay-off.

This means you won't be able to structure your financing around the existing loan because you are paying the loan off. So, you'll either need to come up with new financing yourself, or have a buyer standing by that you can flip the

property to by doing a double closing. If you plan to retail the property, you will usually get the money to payoff the seller's loan from a hard money lender.

## Properties That Are Good Short Sale Candidates

So, what properties are the best candidates for doing a short sale? As we said a minute ago, lenders almost only discount when the seller is behind on their payments. Therefore, the seller should already be at least two to three months behind on their mortgage payments, or already be in foreclosure.

Houses that are ugly can be the best candidates for doing a short sale, mainly because banks don't want to take back a property that needs work, or any property for that matter.

Properties that have very large second or third mortgages make especially good candidates for a short sale, because those second and third mortgages are subject to a very steep discount. If the property goes to foreclosure, chances are those second and third mortgages will get nothing, and they know it. Even if you can't get a discount on the first mortgage, you can still get a major discount on the second or third mortgages, and make a deal for yourself.

## How Much Do I Offer On The Short Sale?

When deciding how much to offer a bank as a payoff, don't try to calculate how much they might take. What the lender will take as a short sale discount has nothing to do with the balance owed on the mortgage. Nor does it matter how far behind the seller is on their mortgage payments, how much it will cost to bring the loan current, or how high the loan-to-value ratio is.

The main determining factor for how much the lender will discount rests almost solely on the lender's BPO appraisal. The letters "BPO" stand for Broker Price Opinion, which is simply an opinion of the property's value done by the lender's real estate broker. If the property is in poor condition and in a bad area of town, the lender will discount more than if the property were to be in nicer condition and in a nicer area. Still, you just never know how much a lender will discount until you start negotiating. Obviously, you should always start low and see how far down the lender will go. Of course, you'll want to be reasonable.

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## Finance Strategies For Selling

Up until now, we've mostly covered the finance strategies used when buying. However, as creative real estate investors, you don't always sell the same way you buy. Certain techniques allow you to keep control over your deal, while other techniques may leave you with little or no control. For that reason, we're now going to discuss which strategies you should use when selling a property and which strategies you shouldn't.

### Flipping

The first strategy we're going to discuss is flipping. This is one of the most popular ways beginning investors get started, because selling a property can be so easy. Best of all, you can buy a property and immediately resell it without needing any money or credit.

There are two different ways you can flip properties. You can either flip ugly rundown houses to other investors below market, or you can flip nicer houses to homebuyers at (or near) retail value.

#### Flipping Wholesale

If you plan to flip houses that need work to investors, you must build a "buyers list" of investors looking to buy investment houses. Building this list of buyers ahead of time is your key to getting the deal sold fast. If you wait until you have found a deal to look for buyers, you may not be able to get it sold fast enough before you have to close.

Another thing to do ahead of time is to find all the money sources you can, who will loan money to investors. This won't necessarily be for yourself when flipping, but you will find it easier to sell your deals if you can help your buyers get financed.

There are a lot of investors out there looking for deals who haven't read this course. Once they find your deal, they will then realize they need creative financing. As you have already learned in the first section, the whole point of this Education is to get your ducks in a row ahead of time so that when you find a deal, you can execute it. This includes being prepared to deal with other investors who aren't so educated.

By the way, we'll be covering how to build these financing sources and contacts later in this module and in the REI Contacts Section.

#### Flipping Retail

Flipping retail houses to homebuyers is a whole different ball game than flipping ugly wholesale houses to investors.

Again, to be successful, you must build a buyers list ahead of time. Obviously, these are buyers who want to live in the areas in which you are trying to buy and sell houses.

Just like with flipping houses to investors, you must know the creative sources where you can get these homebuyers financed. This includes being very knowledgeable about various first time homebuyer loans and down payment assistance programs.

Advanced investors routinely flip houses to homebuyers because they know how to get the buyers financed quickly. In fact, many of their buyers may already be pre-qualified for financing before the investor even finds the deal.

Finally, the properties you will be selling must be in good condition. This means the property should have no "deferred maintenance" which might get noted on an appraisal.

As we just said, flipping retail is mostly done by advanced investors who know the ropes. One way you can test if you have the right skills, is by using an option.

### Flipping Using Options

By using an option, you are able to flip properties with absolutely no risk and best of all, options require almost no money and no credit.

Once you have an option on a seller's property, you have an equitable interest and a right to market the property prior to exercising your option. You can even allow the seller to keep marketing their property themselves. The key here is that you are not obligated to buy. So, if you find a buyer, then great, but if you don't, you haven't lost anything but your time and you would still have gained some more experience.

Realize though, options are not only great to use when flipping nice houses to retail home buyers, you can also use them to flip wholesale deals from one investor to another.

## Retailing

Rather than trying to quick-flip a nice property to a homebuyer, you may decide to buy a rundown property to fix up and resell. This is what we referred to before as the Retailing Deal Section.

Of course, there are a lot of aspects we'll be covering throughout this course about retailing properties. However, the focus right now is the financing behind your sale. After all, if you can't get your retail buyers financed, you won't be able to retail the property.

## Know The Sources For Getting Your Buyers Financed

After getting a property fixed up and on the market, **the hardest part about getting the property sold is finding a buyer who can qualify for financing. The problem is, most buyers you will deal with, will be looking for a home without getting pre-qualified for financing ahead of time.**

As a real estate investor, **it's going to be your job to make sure the buyer gets financed.** You simply can't wait around for the buyer to take care of things on their own.

**The key to getting your properties sold retail is understanding the various financing options a buyer has and getting the buyer qualified for a loan.**

For instance,

- if the buyer is a **"first time homebuyer"**, you must know what first time homebuyer loan programs there are available in your area.
- On the other hand, if the buyer doesn't have much money to put down, **what down payment assistance programs might they qualify for?**
- And finally, if the buyer has **no credit or bad credit**, what loan programs might the buyer still be able to qualify for?

We'll be going into more detail about these financing sources later in this section, as well as how to help them fix their credit if needed.

## Understand Credit Issues

One major issue with getting a buyer financed is their credit, because this is what usually keeps a buyer from qualifying for a loan. **Therefore, you must learn how to assist your buyer in correcting any credit issues which might prevent them from being able to buy your home.**



In fact, most skilled investors are very proficient in the art of credit repair. This is why we have included a bonus chapter in this module on credit repair. You'll need to study that chapter not only for repairing (or strengthening) your own credit, but so you can help your buyers with their credit as well.

## Carrying Second Mortgages

If a buyer has limited credit, they may not qualify for a loan amount sufficient to cover the balance of the purchase price after they put what money they have down.

- For example, if you are selling a house for \$100,000 with the buyer putting down \$5,000 and the buyer only qualifies for an \$80,000 first mortgage ... the buyer will be \$15,000 short.
- **So, to get the deal done, you would have to hold back a seller carried second mortgage for the \$15,000.**

If you're going to be **retailing properties**, there is a good chance you might have to carry back a second mortgage. Therefore, there are some important issues you should know about.

- First, **you should not put a prepayment penalty in your mortgage because you should want the buyer to pay you off early.** It is always better to get your money sooner, than later. So, don't penalize the buyer if they want to pay you off early.
- Any time you take a mortgage back on a property, **make sure the buyer gets a fire insurance policy and names you (the mortgage holder), as "additional loss payee".**
  - This way, if there is any damage to the property or a fire at the property, you know that the insurance company will pay you as a mortgage holder on the property.
  - Also, if the policy is not renewed or is canceled for any reason, you will be notified, at which time you can contact the borrower to make sure the insurance does get maintained.
  - If the borrower does not maintain proper insurance on the property, it is usually standard in all mortgage agreements that you as the mortgage holder can purchase a policy on behalf of the borrower and add it to their mortgage balance.
- You will also want to **make sure that you get a lender's title policy at closing so that you know that your mortgage is properly secured against the property** and
- that your mortgage is protected against any unknown liens or encumbrances.

Finally, **if you want to sell a second mortgage to a note buyer, they usually won't give you much for it, especially if the note has not been "seasoned" for 6-12 months.**

- (By the term "seasoned", we mean how long the buyer has been paying on the note for a period of time.) You can however use these notes as payment to other investors on other deals, or as a down payment to a private seller on another property.

## Lease Options

Another financing technique for selling properties is to sell using a Lease Option.

**This is the only seller financing technique you'll want to use when selling because it gives you the most control over the deal as the seller.**

- You may have bought the property you are selling through any of the creative finance techniques we have covered in this course.
- This includes having bought the property under a Lease Option yourself and you are now looking to **Sub-Lease Option** (second part of the Sandwich Lease Option) the property.
- When selling under a Lease Option, you usually won't be looking so hard for the . tenant-buyer to have good credit, but you will be looking for them to put a sizable amount of money down.

### Giving The Tenant/Buyer Time To Qualify

You'd be surprised how many people out there have a substantial amount of money to put down, but who have trouble qualifying for a bank loan.

There are many reasons why a buyer would have \$5,000 (or even \$10,000) to put down, but not be able to go to the bank and qualify for a loan today. **The most popular reason would be that they had past credit problems, but almost everyone's credit can be cleaned up over time.**

The tenant-buyer may also be **self-employed** and not yet have two years tax returns or they could have a **debt-to-income ratio** problem.

Under a Lease Option, the tenant-buyer would have the time needed for them to clean up any past credit problems and establish new credit.

- They would also have time to increase their income, or to reduce the debts which are affecting there debt-to-income ratio.
- This would allow them to get a purchase loan or refinance loan, down the road.

## Helping Your Tenant-Buyer To Qualify

Selling under a Lease Option is just like retailing a house ... You must understand how to get around any credit issues the tenant-buyer may have and be able to eventually get them qualified for financing.

- When selling under a Lease Option, you won't want to put a tenant-buyer in the property and then leave them to correct any problems they may have on their own.
- You as the seller need to step in and help the tenant-buyer get their credit corrected, so you can eventually get your property sold to them.
- Again, you can use the information and form letters [HERE](#)

## Rent Credits

Along with helping the tenant-buyer with their credit, you can also work with them on building up a larger down payment by giving them a monthly rent credit.

- This is assuming the tenant-buyer did not give you a substantially large deposit on the Lease Option.

**By the way, if the tenant-buyer fails to exercise their option, these rent credits are nonrefundable.**

## Creating A WIN-WIN Situation

You always want to create a win-win deal for everyone by getting a homebuyer into a property at a price and a payment they can afford, while making money yourself.

- However, unless you are planning to give the tenant-buyer long term financing, they should be able to eventually get bank financing if they do everything you tell them to do.
  - Therefore, your mortgage broker should be able to say that the tenant-buyer has a chance of getting refinanced in the future, once certain roadblocks have been corrected. Otherwise, you shouldn't let the buyer into the property.
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## Strategies Not To Use When Selling & Why

As a real estate investor, there are several investments techniques which you can use to buy properties, that you won't want to use when selling properties.

## Assigning Sales Agreements

First of all, when dealing in the Wholesale Section, you can either do a double closing to your new buyer as we discussed earlier, or you can assign your sales agreement to the other investor and let them close the deal.

- However, you'll almost never want to assign your sales agreement unless you have collected all the money you're making on the deal upfront.
- This is because if you assign your purchase and sale agreement to another person, you have just given complete control over the deal to them.
- If they don't close like they are supposed to, you won't be collecting your money at closing, because there won't be a closing.

We have included an **Assignment Of Contract agreement** (3.4) just incase the situation calls for it.

- This would usually be when you're only making \$500-\$1000 on the assignment and the new buyer is willing to pay you all of the money upfront.
- This specially designed Assignment Of Contract also allows for you to take a binder deposit and then complete the assignment only once the assignee has made it to closing.
- We'll be covering more about how to properly use this agreement later on.

## Selling "Subject To" On Your Own Property

**Another strategy to avoid when selling is doing a "Subject To" sale on your own property in which you are the borrower on the underlying loan.**

Unless you are extremely motivated to sell, you won't want to hand over the title to your property and trust the buyer to make your mortgage payments for you.

**It is OK, however, to sell using the "Subject To" technique when you bought the property "Subject To" yourself from another seller.**

## Seller Held Mortgages Or Wraps

For the same reasons we just stated, you won't want to sell under a wrap around mortgage either, if you are the borrower on the underlying loan. It is OK though to sell under a wrap mortgage if you took over the property "Subject To".

**You also won't want to give a seller created first mortgage when selling.** It is much better to "test drive" your buyer first by giving them a Lease Option. This way, you can make sure they'll make the payments like they should, before you hand over the title and take back a mortgage.

- You can simply convert the Lease Option to a seller held mortgage later if you want.
- It is OK, though, to hold "second mortgages" on properties you are selling. This may be especially necessary when dealing in the Retailing Deal Section.

## Contract For Deeds

Finally, you shouldn't sell any of your properties under an Contract For Deed, when you can always structure the deal using a Lease Option.

- Again, by using a Lease Option, you keep more control over the property.
  - For instance with a Lease Option, you'll be in a landlord/tenant relationship. Therefore, if the tenant-buyer doesn't pay like they should, all you have to do is evict them.
  - Whereas under a Contract For Deed, you would most likely have to foreclose on the property you are selling.
  - You would also lose most of your tax benefits by selling under a Contract For Deed.
  - There are just too many other benefits as well with Lease Options that you just don't get when selling under a Contract For Deed.
  - **So remember, it's OK to buy under an Agreement For Deed, but always sell under a Lease Option.**
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## Strategies For Making Money On 100% Financed Properties

In this next section, we're going to talk about making money on properties that are 100% financed.

- By knowing how to **make money on deals which have no equity**, you'll be able to do deals most other investors can't. This eliminates most of your competition.
- There are a lot of sellers out there who want to sell their home, but they don't have enough equity to cover a real estate agent's commission.
- Some may barely have enough equity to even cover their closing costs.
- Most of these sellers are just waiting for someone to come along and provide them with a solution, and that is where you can fit in.

You may be asking ... **"If the property doesn't have any equity, how am I supposed to make any money?"**

Well, there are several ways in which you can make money on a property even if you are paying full market value. They are ...

- buying "Subject To",
- doing an Contract For Deed or Lease Option, and
- doing a short sale.

## Don't Give The Seller Any Money!

One thing to understand upfront about making money on properties which have no equity ... The first way you begin to make money, is by not giving the seller any.

- If the seller owes what their property is worth, there is no reason why the seller should make money on the deal.
- Therefore, the only thing you're going to give them is a solution to their problem.

## Subject To

One way to make money on a property which is 100% financed, is to take over the property "subject to" the existing loan.

- Then, you can Lease Option the property to a tenant-buyer.

You could not only make money by getting an up front deposit, but you can also make money every month by charging a higher monthly payment.

- You can even tie the sales price to a future appraisal.
- This way, you are building up equity in the property until your tenant/buyer exercises their option to buy.
- That equity would be your third payday down the road.

**You could also take over the property "subject to" and then assign the deal to a buyer who wants to live in the property.**

- There are a lot of homebuyers out there who would be willing to pay five or even ten thousand dollars above market value to own a home, if they didn't have to qualify for the loan.

## Contract For Deeds & Lease Options

If the seller is unwilling to deed you their property and walk away, you can offer to do an Contract For Deed or a Lease Option. The important thing here is that the monthly payment you will make, will be the same as the payment on the

seller's underlying loan. Also, the purchase price will be the amount owed on that loan. It is just as if you took over the loan, but the title just gets transferred to you later.

In this situation, you can make money the same way you would if you had taken over the property "Subject To".

## Short Sales

This technique is difficult for a beginning investor, but some experienced investors can do this like a piece of cake.

- If the seller is behind on their payments, it could be a great opportunity to get the lender to do a short sale. This would create equity in the property by the lender taking less than what is owed on the loan. If the property is financed at upwards of 100% of its value, the lender already knows they are going to take a loss.
- It's just a matter of how much of a loss they are going to take, and how much time and money it will cost them in the meantime. If you can get the lender to give a hefty discount, you could come in with private money and close on the deal. You could then do any repairs needed on the property and retail it.

If you're unable to get a large enough discount to use hard money, you would then have to flip the deal directly to a pre-qualified homebuyer. The key here is to get the property sold to a homebuyer quickly before you have to close on the short sale because you don't want to even try to come up with funds anywhere near full price. To do this, you must have a buyers list built up ahead of time and know how to get the buyers qualified quickly for financing.

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## Strategies For Getting Cash Back At Closing

Getting cash back at closing may sound farfetched to some people. However depending on which Deal Section you are working in, you can actually routinely get cash back at closing.

While it is clear that you will get cash back at closing when you wholesale a property, you can also get cash back when buying a property to retail, when refinancing various types of seller financing and when refinancing rental properties. So you can actually get cash back at closing when dealing in each of the four

## Where Does The Cash Come From?

Other courses may give you twenty different ways to get money back when you buy a property, but it doesn't have to be that complicated.

All you need to understand is where the money comes from.

Then you can very easily structure your financing technique to the deal's unique situation, rather than waiting for a deal's situation to match a very specific finance technique.

So, the cash you get back at closing has to come from somewhere, but where?

**Simply put, there are only three places it can come from ... the seller, money you borrow, or your buyer.**

## The Seller

The first source for getting money back at closing is the seller. Few sellers will ever come to closing with cash and pay you to take over their property, but it does happen on very rare occasions. There are also a lot of hair-brained ideas out there such as getting the seller to refinance and give you the cash, but these things virtually never happen.

## Rental Deposits & Closing Credits

One instance when a seller would bring money to closing, is when the seller is holding the security deposits from any tenants that are in the property.

- When you purchase a property which is already rented out, you as the buyer must get a credit from the seller for the security deposits, last month rent payments, and even current month rent payments.
- Remember, rent is almost always due at the beginning of the month. So you'll want to make sure all the regular rent payments are at least prorated as of the date of closing.
- You could even negotiate for all of that month's rent.
- If the property has multiple rental units, these monies can add up to quite a bit, especially if you're buying a large apartment complex.

**Unpaid property taxes will also be credited towards your costs, but remember, those taxes must be paid at the end of the year.** All of these items are commonly referred to as "Closing Credits" and are credited on your closing statement.

## Money You Borrow

The most common way to get cash back at closing when you buy a property, is to borrow more money than is needed to cover your purchase price and closing costs.

## Wholesaling To Yourself Or Your Partnership

One of the easiest ways to get cash back at closing is by borrowing money from a hard money lender. These hard money lenders routinely lend out money based on the property's "after repaired value" and not based on your purchase price.

Basically, instead of wholesaling the property to another investor (who will fix the property up and either retail it or keep it as a rental), you are going to wholesale the deal to yourself. To do this, you simply borrow more money than what you're buying the property for. After fixing the property up, you would then either keep it as a rental or retail it.

You can also wholesale a deal to your partnership. There is no reason why you can't make a few bucks upfront for finding a deal. If this is the case, make sure your partner knows what you're doing. Otherwise, they may get upset and feel as though you took advantage of them if they find out after the fact. Just remember never to get greedy and to always be honest.

You may also need to use this technique if you are working with numerous partners at one time. For instance, you may work with one partner to find a deal, and then wholesale the property to another partner in which you will work with to retail the property.

## Refinancing Rental Property

Another way to get money back at closing that you borrow, is to refinance a property for more than you owe. This is commonly referred to as a "cash-out refinance".

These "cash-out" refinance loans can be received through just about any mortgage broker around the country. Realize though, when getting cash-out on a rental property, this is called a "**non-owner occupied cash-out refinance**". To get this type of mortgage loan, you must have good credit and the mortgage payments on the loan you are refinancing must have been paid on time every month for at least 12 months or more. The rental income from the property must also be well documented.

**There are some side affects to borrowing extra money on a rental property.**

First of all, **the extra money you get increases your loan balance.** This in turn **increases your monthly mortgage payment, which reduces your monthly cash flow.**

Remember, the objective with owning rental properties is **to have a monthly residual cash flow which you can use to become financially free.**

- Also, everything you borrow must be paid back eventually.
- This will either be on a monthly basis out of your cash flow, or out of your sales proceeds if you decide to sell the property before the loan is paid off.

Secondly, **if you get any money out, the interest rate on your loan will get bumped higher.** Usually, the rate bump would be anywhere from a **half of a percent, to one whole percent.**

Realize too, you would **also be paying the higher rate on the extra money you borrowed.**

## Your Buyer

Finally, the money you get from closing can also come from your buyer. **We're not talking about getting money back at closing when you sell a property you already own; but rather, flipping properties and getting money back at closing.** After all, you walk in the door of closing agent's office not owning the property, and you walk out the door with the property sold and a check in your hand.

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## Financing Sources

As we discussed at the beginning of this Section ...

The Money Section consists of two main sections. Those two sections are "**financing strategies**" and "**financing sources**".

Up until now, we have covered many of the financing strategies used to invest in real estate. Now, let's take a closer look at some of the financing sources there are.

As a real estate investor, you have a wide range of financing sources. These sources can be broken down into "**traditional sources**" and "**nontraditional sources**".

Traditional sources of financing would be mortgage brokers, banks and other financial institutions.

Non-traditional sources of financing would be seller financing, partners, hard money lenders, or even credit cards and lines of credit.

As a real estate investor you are going to deal a lot with these non-traditional sources.

As we cover the various financing sources, you may decide that some sources fit your needs while other sources don't. However, you must know all the financing sources there are, not only for yourself, but also for your buyers. It is very important to know how and where you can get your buyers financed.

By knowing where to send your buyers, you'll make it easier for the buyers to purchase your properties, which in turn, will make it easier for you to unload deals faster.

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## The Seller As A Source Of Financing

The first source you should always try to get financing from is the seller. This is assuming the seller is a private owner and not a lending institution.

As we have already discussed, there are many forms of seller financing, including wrap around mortgages, seller held second mortgages, "Subject To", Contract For Deeds, and Lease Options. However, there are some more creative financing techniques you can use when dealing with seller held mortgages.

For instance, if you got the seller to hold all of the purchase price as a seller held mortgage and you didn't put any money down, you would think the seller couldn't get any money at closing, right? After all, where would the money come from? You're not putting any money down and you're not getting any money from an outside financing source. The answer is ... the seller can sell all or even just part of a seller held note.

## Simultaneous Financing

One creative financing technique is referred to as a "simultaneous closing" or "simultaneous financing". Using this technique, you would line up the sale of the seller's entire note prior to closing. The reason this technique is referred to as "simultaneous financing", is because the seller will create the seller held note, and then simultaneously sell the note at closing to get cash.

The process starts after the seller has found a buyer. The note buyer will usually first look at the buyer's credit, employment history etc. The note buyer will then make a recommendation as to what the interest rate should be on the seller held note along with the loan amount and other terms based on the type of note the note buyer is looking to buy. This recommendation by the note buyer is also determined heavily by the property's value, the sales price, and the amount of money (if any) the buyer is putting down.

Once the note buyer, seller and home buyer have all agreed on the terms of the seller held financing, a closing can be scheduled. After all the closing documents have been signed, the note buyer will wire funds to the closing agent for the purchase of the seller held finance note.

Because most note buyers are looking to make 12-15% on the notes they buy, the seller will almost always have to sell the note below its face value. This is referred to as the "discount". Also, many note buyers won't buy above 75% of the properties value. Therefore the seller may have to create two notes. The first mortgage note could be for the 75% a note buyer is willing to purchase, and the other could be a second mortgage note for 25% which the seller would keep. In this case, the seller could get the majority of the sales price now, and then have a small monthly cash flow off the second note they kept.

## Selling Note Payments

Rather than doing a simultaneous closing where the seller sells their entire note, the seller could also just sell a portion of the note. If a seller owns a property free and clear you can give them a mortgage for up to 100% of the purchase price. The seller would then sell a portion of the note so they can receive the amount of cash they want now.

To do this, first determine how much cash the seller actually needs along with the loan amount, interest rate, term and payment amount on the note you will be creating. Then use a financial calculator to calculate how many payments the seller must sell to receive the amount of cash they want now.

As an **example of calculating a note discount**, most note buyers are looking to make 12-15% on the payments they buy.

Therefore, if you had a \$100,000 note at 10% interest for 30 years, the payment would be \$877.57.

For the seller to receive \$10,000 now, they would have to sell roughly 12 payments which all together would total \$10,530.84.

Remember, the note buyer is looking to get upwards of a 15% yield and the note only has an interest rate of 10%.

### **This is why there is a need to discount the payments.**

- To account for the discount the seller must take on the note, you can increase the loan amount and/or increase the interest rate.
- This will allow the seller to get more money at closing if needed.
- It is important when negotiating with the seller, to show them how much is still owed on the note after the note buyer has received their payments.
- In the above example, after the note buyer has collected the first 12 payments, the seller would begin collecting the remaining payments on the note.
- However, even though the note buyer collected over ten thousand worth of payments, the amount still due to the seller on the note is \$99,444.12.
- That's right, the seller can get \$10,000 now and after 12 months, they are still owed almost the entire original amount!

It will be surprising for most sellers to find out they will still be owed very close to the original amount in such a scenario. This is due to the fact that the mortgage payments are mostly for interest in the beginning and are paying down very little principal. By the way, the seller can sell off more of the note any time they want cash right away and you can even use this strategy for selling your own property.

## **Selling Payments On A Second Mortgage**

If you are giving the seller a second mortgage, it would be very difficult for the seller to resell that mortgage or any of the payments to a note buyer, because of its secondary position.

**The reason is, if the buyer defaults on the first mortgage, the first mortgage could foreclose and wipe out the second mortgage. The only way to prevent this would be if the owner of the second mortgage assumed responsibility of the first mortgage. Most note buyers are not willing to deal with this issue, so they steer clear of second mortgages.**

Also as we said earlier, most note buyers will not buy above 25% of the properties value. This upper 25% is where most of your second mortgages are.

## **Selling Payments From A Wrap Mortgage**

Selling payments on a wrap around mortgage is just like selling payments on a second mortgage. There is still an underlying first mortgage which must be dealt with. Therefore, you cannot sell payments from a wrap mortgage.

If the seller has underlying financing and does not own the property free-and-clear, consider doing simultaneous financing. In this case, the money the seller gets when they sell their note would payoff the underlying financing.

## **Future Discounting**

When dealing with seller carried mortgages, there is another profit center for you as the borrower and that is **future discounting**.

- Any time you pay a note off early, you should always ask for a discounted payoff. After all, money today is always worth more than collecting payments over time, and it doesn't matter if you owe the seller on a first mortgage, second mortgage, or a wrap around mortgage. Also, the more you owe to the seller, the larger the discount you may be able to get.

When you go to refinance, or when you have the property resold, **simply approach the seller and say that you are coming into some money which you could use to pay them off, if they are willing to discount how much you owe them.**

**It is very important not to let the seller know that you are definitely refinancing or that you have the property sold.**

- In either of these two cases, the seller would know they are going to get paid off no matter what. Therefore, there wouldn't be any motivation for the seller to take a discount.
- The key is to make the seller think you are getting money off another deal and if they don't discount, you plan to invest the money you are getting into something else.

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## **Bank Financing**

If you can get a bank loan to purchase a property, then great.

However, this instruction is not based on the idea that you should go out and get bank loans to purchase property.

- The only times you as an investor should ever be going to a bank for financing, is to refinance a hard money loan on a rental property when you plan to hold onto it long term, or to get financing for one of your retail buyers.

## Important Issues Regarding Conventional Bank Financing

There are a lot of limitations regarding conventional bank financing that you should be aware of whether you are a homebuyer or an investor, and we're not just talking about credit or having money to put down. **In this section we will cover many of the problems you will run into with bank financing and how to get around them.**

### The Term "LTV"

First is the fact that almost all bank mortgage loans are based on the purchase price and not the property's value. A common term you will hear in real estate is "LTV", which stands for "Loan To Value". This refers to the percentage of the property's value that the bank will lend up to. However, even though the letters "LTV" stand for "Loan To Value", banks almost always lend according to the purchase price.

For instance, let's say you are buying a property for \$95,000 and it is worth \$100,000. Under a 95% LTV loan, the bank would only lend \$90,250 based on the sales price. So, even if a bank says they can do a 95% LTV loan, this actually means they will only lend up to 95% of the sales price, not 95% of the true value of the property. The only time a bank tends to go by the actual "value" of the property, is if you are refinancing.

### Seasoning Issues

Probably the biggest problem you will have with bank financing is "Seasoning". As we said before, seasoning is the amount of time an owner has owned a property before they resell it or refinance it. This is also commonly referred to as "seasoning of title" because you are referencing how long the owner has held title in their name.

As an investor, you will quickly find that seasoning issues are a major obstacle. How long you have owned a property will usually be a factor when you retail properties or try to refinance a rental property.

When dealing in the Retailing Deal Section, you must have financing sources which don't require you to own the property for an extended period of time before reselling it. Banks don't like to see investors buying houses at a discount and then reselling them a few months later at a higher price. Even if the property needed major rehabbing, the banks feel the original price you bought it for would be about what they would get if they had to foreclose and resell the property.

**When getting your retail buyers financed, most banks will look for twelve months seasoning.** Again, this means you must own the property for twelve months before you sell it. Some banks will look for only six months seasoning. This probably won't be a factor if it took you five or six months to fix the property up and find a buyer.

There are however a few banks which don't require any seasoning. It is these banks that you must find and add to your list of financing sources. To find such a lender takes a lot of calling around to various banks and mortgage brokers, and searching online.

One way most investors avoid the issue of title seasoning is to get their buyers financed with an FHA loan, because FHA loans do not require seasoning. They do require you as the seller to pay a lot of extra closing costs and the property must be able to pass an FHA inspection.

Another way around the seasoning issue is to Lease Option the property to the buyer for twelve months. This may or may not be a good idea depending on your particular situation and the deal itself.

The other time you will have to consider seasoning is when refinancing a rental property. Again, most banks look for six to twelve months of seasoning before you can get a refinance loan, but some will do a refinance loan with no seasoning. To get the best rate and terms on your new loan, it is best if you own the property for twelve months before refinancing. This allows you to create a payment record on your existing loan and allows you to show that the property can produce a sufficient cash flow.

### Chain Of Title

Another term you will hear as an investor is the term "chain of title". The "chain of title" on a property is the list of people who have owned it. Kind of like a chain linking one previous owner to the next. This term should not be confused with the term "seasoning of title" because it has nothing to do with the amount of time someone has owned the property. It only has to do with the fact of someone actually showing on title as either owning the property or having owned it in the past.



This term mainly applies when you are doing deals in the Wholesaling Deal Section. If you buy a property and then wholesale it to another buyer ... if that buyer is getting bank financing, the bank will most likely require you to show in the chain of title. The problem arises when the buyer applies for a loan with a bank on the house they are buying from you. However, when the bank has a title search done, you don't show on title because you haven't bought the property yet.

For the bank to be able to sell the mortgage on the secondary market, you must show as a previous owner. To do this, you must do a double closing which will show you in the chain of title. Realize though, if you show on title as the owner who is selling the property to the buyer, you will only own the property for a few brief minutes on the day of the double closing. This means that the bank must not have any seasoning of title requirements as we discussed earlier.

To get around the chain of title issue, you can simply assign your purchase and sale agreement to the new buyer for a fee. The only problem with this is that the buyer's loan amount will be based on the lower sales price you had with the actual owner. Also, your assignment fee won't be able to get included within the new buyer's loan amount, which means the buyer will have to come out of pocket with more money.

## **Bank Financing For Investors**

If you are an investor trying to get conventional bank financing, there are some more issues to understand other than just dealing with seasoning issues and the chain of title.

### **Non-Owner Occupied Loans**

First of all, any time you get a loan on an investment property, that loan is referred to as being "non-owner occupied". This is because as the owner, you won't be occupying the property. These non owner occupied loans are much harder to qualify for than if you were qualifying for an owner occupied loan.

Banks know that people pay their home mortgage first, and investment properties (and other bills) are always paid second. In other words, if an investor gets into financial trouble, the investor may stop paying on their investment properties, but they will most likely keep paying on their home mortgage because they need a place to live. Therefore, non-owner occupied loans are defaulted on more often and are considered a higher risk.

As a result of the higher default rate and risk on non-owner occupied loans, banks charge higher interest rates and look more closely at the borrower's credit and job history. So if you are an investor planning to get bank financing on any of your investment properties, be prepared to be scrutinized a little more closely than if you were applying for a regular home loan.

### **Banks Will Cut You Off**

Another issue when getting numerous non-owner occupied loans is that banks may begin cutting you off from more financing. Some banks have a company policy of only having out four or five loans to one individual at one time. This is to help reduce the bank's risk in case the borrower goes bankrupt. You may find a particular lender with a great loan program you can qualify for over and over. If this is the case, be sure to check as to whether or not the bank has a limit on the number of loans they will make to you.

Banks may also deny your loan application if they see you have borrowed several new loans recently. This is because many new investors go diving into real estate investing and get in over their heads. Also, many investors will begin refinancing all of their properties when they are having financial problems in an effort to liquidate some of their equity. As a result, banks consider you to be a higher risk if you are borrowing lots of money within the last six to twelve months. So keep this in mind if you are planning to purchase or refinance several properties within a short period of time.

### **Leveraging Both Spouse's Credit**

To help alleviate the problem of banks cutting your financing off, if you are married, you and your spouse should borrow money separately.

One spouse can use their income, job history and credit to qualify for a series of loans. This leaves the other spouse's credit open for doing separate loans. By each spouse qualifying for loans separately, you increase your collective ability to leverage your way into owning more investment properties. After all, teamwork is part of marriage and it can be part of your financial strategy together as well.

The title can still be in both spouse's names, or in the name of a land trust. The key is to only use one spouse's credit to qualify for the loan. Just because a couple is married or owns the property together, does not mean that both have to qualify for the loan.

If both spouses are on title together, the other spouse would be required to sign on the mortgage which secures the loan against the property. That spouse would not have to sign on the note which is the guarantee of payment on the

debt. It is important that you understand when both spouses have to sign and when they don't. It is also important that you make it very clear to the bank upfront that only one of you is qualifying for the loan.

## **Your Debt-To-Income Ratio**

When buying rental properties, it is important to understand how owning the property can affect **your debt-to-income ratio**.

Your debt-to-income ratio (or DTI ratio as it is commonly called), is calculated by dividing your monthly expenses per month by your gross income per month. For instance, if you make \$4,000 per month and your monthly credit card payments and mortgage payments add up to \$2,000, your DTI ratio is 50%.

To be included as part of the debt ratio, the debt must be fixed and have payments due for more than six months into the future. So, if there are less than six months worth of payments left, the debt does not get included. Also, the only payments you should consider when calculating this ratio are the payments which show on your credit. Money for food, clothing, electric bills and so on, are not part of this calculation.

Whether you are buying a home to live in or buying an investment property, banks will look at your "front end" ratio and your "back end" ratio. The front end ratio is your DTI ratio before you buy the property, and the back end ratio is what your DTI ratio looks like after you buy the property.

If you were a home buyer, you would have more debt after buying the property. Therefore, your back end DTI ratio would be higher. If it were to be too high, the bank would not give you the loan for fear you could not afford the payments.

On the other hand, as an investor buying rental properties, your back end DTI ratio should actually be better after you buy the property. This is because you should have more rental income coming in than what your payments on your loan are. One problem is that most banks only give you a 75% credit for the rental income. This is to allow for vacancies and repairs. So, if the property currently has a rental income of \$1,000, the bank will only give you a credit of \$750 when calculating your ratio.

By only getting a 75% credit for the rental income, your back end ratio could actually go up instead of going down. This is something to consider if your front end ratio is already a little high.

## **Refinancing Rental Property**

If you are refinancing a rental property, there are some other items to consider.

First, most refinance loans are based on the properties value and not your original purchase price. This is helpful to you as an investor if you have a lot of equity.

For instance, if the property is worth \$100,000 and the bank will lend you 80% of the property's value, you'll be able to borrow \$80,000. If you only owe \$70,000, you could walk away from closing with \$10,000, minus your closing costs of course. This is what is called a "cash-out refinance" because you are cashing out part of your equity.

Any time you get cash-out at closing, the bank will usually bump your interest rate a little higher. In this case, you must consider how much the higher interest rate will cost you not only monthly, but in the long run. You'll want to compare this cost to how much cash you're getting out to determine if getting the money is really worth it to you. This can especially be important if you are only getting a few hundred dollars. It doesn't matter to the bank if you are getting just a little bit of money. If you're getting even \$1 cash-out, your rate still goes up the same as if you had gotten \$10,000.

It is important to find out if the bank will consider any money you have put into the property as being part of the refinance. In the example we gave a minute ago, if you bought the property for \$70,000 with no money down and subsequently put \$10,000 into fixing up the property ... will the bank allow you to get your \$10,000 back without considering the money to be "cash-out"? This is especially important if you only qualify for a "no cash-out" loan program or if you want to keep your interest rate down. By the way, keep all receipts for your rehab expenses so you can prove to the bank how much you put into the property. Of course, you'll need those receipts for your tax records as well.

One advantage to getting cash-out on a refinance is that the money you get from a refinance is not taxable because it is money from a loan you must pay back. Any money which must be paid back can not be considered as true income for tax purposes.

You should also be careful when considering any money you get as spendable income. The money you get from a cash-out refinance should be wisely invested. Remember, if you spend the money, after it is gone you will still have to pay it back either out of your monthly cash flow or when you sell the property.

## **Don't Stop Making Your Payments!**

One mistake some investors make is, they think they don't have to make the payments on their existing loan just before they refinance.

They figure the past due payments can get rolled into the loan payoff and get paid at closing out of their refinance loan proceeds. Absolutely do not do this!

If you are refinancing a bank loan, the past due payments will show on your credit report. Furthermore, the bank doing the refinance loan will perform a Verification Of Mortgage (VOM), and if they find you are past due on your payments, they may cancel your loan. Even if you are pre-approved for the new loan, the bank can always take that approval away.

If your existing loan is with a private lender, the private lender may get uncomfortable with the fact that you stopped making your payments. This could affect your ability to get another loan from the private lender in the future on a new deal.

### **Don't Quit Your Day Job!**

Don't quit your day job just before you go to closing on a refinance either.

Again, the bank may do a Verification Of Employment (VOE). Even if the bank has already received a written VOE from your employer, the bank may call to make sure you are still employed either the day before (or the day of) closing.

## **Bank Financing For Homebuyers**

When it comes to bank financing for homebuyers, there are many important issues to understand, whether you are getting a bank loan for yourself or helping your buyer to get a bank loan. Understanding how to get buyers financed is essential as a real estate investor. You must know what various bank loan programs are available, especially the programs which require little money down or which have limited credit requirements.

### **First Time Homebuyer Programs**

If you plan to retail property, you'll want to focus on learning about the various "first time homebuyer" loan programs that are available. This is also the type of loan you'll want to look into if you are buying your first home for yourself.

Under these loan programs, a buyer can get into a home with around 3%-5% down and some programs may even give 100% financing. As part of qualifying for the loan, buyers may be required to take a class or complete a workbook about being a home owner.

### **Government Assisted Programs**

There are also a lot of various government programs available. This includes state and county "bond programs" or "head start" programs. Under these programs buyers can get assistance for their down payment and/or closing costs.

If you are looking to buy a home, these programs may be of great assistance to you. If you are planning to deal in the **Retailing Section**, knowing how to help push your buyers through these programs will make it much easier for you to get your moderate and low income properties resold.

### **Low Doc and Stated Loans**

Other types of loan programs to look into are "low doc" and "stated income" loans. "Low doc" stands for "low documentation". This means the bank won't require as much employment and credit verification as part of the loan application. "Stated income" loans allow a borrower to state how much money they make and how long they have been on the job, without having to provide proof or the bank verifying the income.

These types of loans programs can be very helpful when a buyer can't prove their income, they have a limited job history, or have minor past credit problems such as being late on their house payment in the past 12 months. Of course, these types of loans carry a little more risk for the bank. Therefore, the interest rate will tend to be higher and the buyer may be required to put more money down.

### **FHA Loans**

FHA insured loans are also a great program to understand if you'll be dealing in the Retailing Section because you won't have to worry about seasoning issues like you would with other programs.

FHA loans do have a lot of closing costs associated with them that must be paid by the seller. So, if you are selling your property to a buyer who will be getting an FHA insured loan, be aware that you'll be paying most of the closing costs in connection to your buyer's loan.

## **Buyer's Down Payments**

As for down payments, most bank loan programs require the borrower to put money down when purchasing a property. If the borrower does not have enough money as required, there are several ways you can help them as the seller.

Giving or loaning the down payment to the buyer is fraudulent and illegal. But, you can buy something from them such as a car, boat, RV, etc. You can also pay them to work on a **different** property you may own. Of course, how much you pay them to work on one of your other properties is up to you, but paying them to work on the property they are buying would be considered "**sweat equity**" and won't be able to be used towards their down payment.

Even though you as the seller can not gift the buyer part of their down payment, one of the buyer's relatives can. Most banks will want to verify that the relative actually had the money. Therefore, the relative must be able to show how or where they got the money to begin with.

If the deal allows for it, you could help the buyer build up a down payment by Lease Optioning the property to them.

Always remember though, you must be able to prove the buyer paid you the money towards the down payment, no matter how the buyer pays it to you.

### **Seller Concessions For Closing Costs**

Besides the money the buyer may need as a down payment, you must also consider any money the buyer will need for closing costs. Sometimes, the seller may be willing to pay all the closing costs; however, some banks limit the amount of closing costs the seller can pay on behalf of the buyer. These extra closing costs the seller pays is referred to as "seller concessions".

If you are the seller of a house, you need to make sure the bank who is giving the buyer a loan will allow you to pay most or all of the closing costs. This is assuming that the buyer is short on the amount of money they need to come to closing with.

If you are the buyer on a house, you could offer the seller a few hundred dollars more on the price of the house in exchange for the seller paying more of the closing costs. Again, make sure of how much the bank will allow the seller to pay in concessions.

### **Refinance A Lease Option**

Another type of loan program to have at your disposal are the programs which allow a tenant/buyer under a Lease Option to refinance their lease as if it were seller financing. By the bank treating the Lease Option as seller financing, the buyer is able to get a refinance loan rather than a purchase loan. This is easier to qualify for and requires less out-of-pocket money from the buyer. Some banks will even look at the value of the property rather than the purchase price, which might allow them to borrow more money than what is owed on their Lease Option.

One of the reasons it is a whole lot easier to get a buyer refinanced than to get them a straight-out purchase loan is because the buyer can show the bank that they are capable of making monthly payments on time and that they are capable of handling the ownership of the home.

Many lenders are very concerned about the buyer defaulting before they even make their first payment, especially if the lender knows that the property is being bought from an investor. This is because sometimes investors will pay people to be a "**straw buyer**".

As we discussed before, a straw buyer is basically a person who purchases a property and borrows the money so that the investor can get cashed out. The buyer has no intent of ever making a payment or even taking possession of the property and some investors may even use bogus appraisals which have an inflated property value.

As an investor who is selling properties under a Lease Option, you must know what the banks are looking for when it come to **credit, job history, and money down**.

This will help you to pre-qualify prospective tenant-buyers to make sure you get a buyer who has the highest chance of getting refinance later. Having a good understanding of these programs also helps you in knowing what credit issues you'll need to help the tenant-buyer correct and you'll know how much money the tenant/buyer will need to build up towards their down payment.

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## **Mortgage Brokers**

Sometimes, figuring out which bank has the best loan program for a particular situation can be a daunting task. That is why many homebuyers and investors use the services of a mortgage broker.

A mortgage broker's job is to take the borrowers loan application and shop it around to various lending institutions and hopefully get them the best rate and terms available. The mortgage broker acts as a middle-man between you and the lending institution and they will handle most of the paperwork for you or your buyers. One of the most important things they will do is work to make your loan application (or your buyer's loan application), look the best it can. As a result, many times mortgage brokers can get buyers qualified for financing who otherwise would not qualify at a local bank.

Mortgage brokers interview lending institutions and search out which ones will loan money on rental properties, which ones have the best first-time home buyer programs, which ones will allow you to get cash back at closing on a refinance, and so on. Some mortgage brokers also specialize in FHA or VA financing and some brokers even have private individuals who will make hard money loans to investors. We will talk about this type of broker more in just a little bit.

## What Is A Normal Brokerage Fee?

The fee a mortgage broker charges can be any number of things. It could be a flat rate ranging anywhere from a few hundred dollars to as much as several thousand dollars. It could also be a percentage of the loan amount. A lot of what determines the fee is the type of loan being applied for and how hard the broker will have to work to get the borrower qualified.

When agreeing on how much a broker will make, you should be aware that the broker can make money on what is called the "back end" through junk fees and kick-backs from the lender.

### Beware Of Par Plus Pricing

The first thing to watch out for is a thing called "**par pricing**". Many lending institutions will pay the broker extra money in exchange for the broker giving you a higher interest rate. That's right, the broker can stick you with a higher rate just so they can make some extra money. So, always make sure you are getting the best rate and that the broker is not trying to make extra money on the back-end.

Many times, this extra money will not be disclosed until closing. Even then, the lender and broker will slip the figure into the closing statement, **usually off to the side of about lines 800 through 802 of the HUD1.**

Next to the dollar amount the broker is getting from the lender as a **kick-back**, will be the letters "**POC**".

**This means "Paid Outside of Closing".**

**To prevent any problems, you should discuss par pricing when making your application and anytime the broker gives you a quote from a particular lender.**

**You can however use par pricing to your advantage.**

For example, **you can lower your closing costs by having the mortgage broker reduce their brokerage fee.**

- Then, the broker can increase the interest rate on your loan and make their fee on the back-end.

### Ask About " Junk Fees"

You'll also want to ask about the "junk fees" that are involved.

- Some of these fees come from the mortgage broker and others may come from the lending institution itself.
- Some of the fees are for processing, curriers, document preparation, document review, faxing, and anything else they can think to charge for.
- Most of these fees are just there so that the bank (or mortgage broker) can make an extra buck.
- The problem is, all these extra fees can add up to several hundred dollars very quickly, so be sure to ask about them upfront.
- Usually, you won't be able to negotiate with the lender about their fees because they are pretty much set in stone.
- However, you can negotiate with the mortgage broker on their junk fees.
- The biggest and most common junk fee is the processing fee.
- If you're going to be charged a processing fee, ask who the processor is.
- This fee is normally charged for an outside processing company.
- However, many mortgage brokers charge this fee even though they are the one who is doing the processing.
- If this is the case, the fee is nothing but an attempt to make more money on your loan.

**The fees a good mortgage broker charges can be well worth it as long as the fees are reasonable and everyone knows who is making what.**

## Pre-Qualifying Your Buyers

As an investor, one of the most valuable things a mortgage broker can do is help you to pre-qualify your retail buyers. The broker will meet with your buyers, pull their credit and let you know if the buyer will qualify for a loan to purchase your property.

Afterwards, the broker will work to clean up any minor problems with the buyer's credit, polish their application package and submit it to the bank.

Many times, the mortgage broker will also make title requests, order appraisals, order inspections, and help you to schedule the closing. These services are well worth the brokerage fee they charge. Remember, it is your job to be a real estate investor who buys and sells houses. So, don't let yourself get tied down with trying to do the mortgage broker's job on your own.

## Get Pre Qualified Yourself

You'll also want to get with a mortgage broker to get pre-qualified for financing yourself. This is an important step to do before you go out looking for properties or making offers.

You must know where you can get financing from and for how much, BEFORE you go out looking for deals. You don't want to go out and find a deal, and then not be able to close on it. This is one of the main concepts of why the Money Quadrant is first, and the Real Estate Quadrant is last. Yes, some deals can be done without the need for new financing. However, you won't know this until the deal is in front of you. So line up your financing ahead of time and you'll be prepared no matter what type of deal comes your way.

Start by getting with an experienced mortgage broker to find out what particular loan programs you will (or will not) qualify for. The best thing to do is to check with a broker and see if you can qualify for both a purchase loan, as well as a refinance loan. Sometimes, a particular deal may require you to get a new purchase loan. Other times, you may be able to get a short term Agreement For Deed or Lease Option, in which case you could get a refinance loan later. So be sure to get pre-qualified for both scenarios ahead of time.

At the same time, your broker should be able to give you an idea of what the maximum percentage loan amount could be both dollar-wise and percentage-wise. In other words, you may qualify for an 85% loan-to-value loan, but you will also have a limit on the total loan amount and monthly payment you can afford.

You'll also want to ask your broker what credit issues may affect your chances of getting qualified and if your credit needs to be strengthened or fixed prior to refinancing. This can give you a chance to work on your application before you really need it.

## Pre-Qualification Letter

Another good thing about getting pre-qualified ahead of time is that the mortgage broker can give you a pre-qualification letter. You'll sometimes need this letter when making offers through real estate agents or on bank owned properties.

## Loan Pre-Approval Vs. Final Loan Approval

There are some important issues to understand about a mortgage broker saying that you (or your buyer) is approved for a loan.

When getting financing through a mortgage broker, the mortgage broker will submit your information to a lending institution under a certain program. The bank will then issue a "conditional loan approval". This means the lender is approving the loan according to the application that was submitted. However, there are still contingencies which must be met and information that must be submitted prior to getting a final approval and closing. It is these conditions and additional documentation that you - have to worry about. They range anywhere from the title simply coming back clear, - to major credit issues which must be resolved ahead of time. All these contingencies must be signed off on by the lender; otherwise, you (or your buyer) do not have a loan.

Once all the contingencies have been met, the lender will issue a "Final loan approval". This means you can actually go to closing but even then there is always a chance that something could go wrong or get canceled. All-in-all, never consider yourself or your buyer approved for a loan until you are sitting at the closing table signing the closing documents.

Up until now, we've mostly covered the finance strategies used when buying. However, as creative real estate investors, you don't always sell the same way you buy. Certain techniques allow you to keep control over your deal, while other techniques may leave you with little or no control. For that reason, we're now going to discuss which strategies you should use when selling a property and which strategies you shouldn't.

## Flipping

The first strategy we're going to discuss is flipping. This is one of the most popular ways beginning investors get started, because selling a property can be so easy. Best of all, you can buy a property and immediately resell it without needing any money or credit.

There are two different ways you can flip properties. You can either flip ugly rundown houses to other investors below market, or you can flip nicer houses to homebuyers at (or near) retail value.

## Flipping Wholesale

If you plan to flip houses that need work to investors, you must build a "buyers list" of investors looking to buy investment houses. Building this list of buyers ahead of time is your key to getting the deal sold fast. If you wait until you have found a deal to look for buyers, you may not be able to get it sold fast enough before you have to close.

Another thing to do ahead of time is to find all the money sources you can, who will loan money to investors. This won't necessarily be for yourself when flipping, but you will find it easier to sell your deals if you can help your buyers get financed.

There are a lot of investors out there looking for deals who haven't read this course. Once they find your deal, they will then realize they need creative financing. As you have already learned in the first section, the whole point of this Education is to get your ducks in a row ahead of time so that when you find a deal, you can execute it. This includes being prepared to deal with other investors who aren't so educated.

By the way, we'll be covering how to build these financing sources and contacts later in this module and in the REI Contacts Section.

## Flipping Retail

Flipping retail houses to homebuyers is a whole different ball game than flipping ugly wholesale houses to investors.

Again, to be successful, you must build a buyers list ahead of time. Obviously, these are buyers who want to live in the areas in which you are trying to buy and sell houses.

Just like with flipping houses to investors, you must know the creative sources where you can get these homebuyers financed. This includes being very knowledgeable about various first time homebuyer loans and down payment assistance programs.

Advanced investors routinely flip houses to homebuyers because they know how to get the buyers financed quickly. In fact, many of their buyers may already be pre-qualified for financing before the investor even finds the deal.

Finally, the properties you will be selling must be in good condition. This means the property should have no "deferred maintenance" which might get noted on an appraisal.

As we just said, flipping retail is mostly done by advanced investors who know the ropes. One way you can test if you have the right skills, is by using an option.

## Flipping Using Options

By using an option, you are able to flip properties with absolutely no risk and best of all, options require almost no money and no credit.

Once you have an option on a seller's property, you have an equitable interest and a right to market the property prior to exercising your option. You can even allow the seller to keep marketing their property themselves. The key here is that you are not obligated to buy. So, if you find a buyer, then great, but if you don't, you haven't lost anything but your time and you would still have gained some more experience.

Realize though, options are not only great to use when flipping nice houses to retail home buyers, you can also use them to flip wholesale deals from one investor to another.

## Retailing

Rather than trying to quick-flip a nice property to a homebuyer, you may decide to buy a rundown property to fix up and resell. This is what we referred to before as the Retailing Deal Section.

Of course, there are a lot of aspects we'll be covering throughout this course about retailing properties. However, the focus right now is the financing behind your sale. After all, if you can't get your retail buyers financed, you won't be able to retail the property.

## Know The Sources For Getting Your Buyers Financed

After getting a property fixed up and on the market, **the hardest part about getting the property sold is finding a buyer who can qualify for financing. The problem is, most buyers you will deal with, will be looking for a home without getting pre-qualified for financing ahead of time.**

As a real estate investor, **it's going to be your job to make sure the buyer gets financed.** You simply can't wait around for the buyer to take care of things on their own.

**The key to getting your properties sold retail is understanding the various financing options a buyer has and getting the buyer qualified for a loan.**

For instance,

- if the buyer is a **"first time homebuyer"**, you must know what first time homebuyer loan programs there are available in your area.
- On the other hand, if the buyer doesn't have much money to put down, what down payment assistance programs might they qualify for?
- And finally, if the buyer has no credit or bad credit, what loan programs might the buyer still be able to qualify for?

We'll be going into more detail about these financing sources later in this section, as well as how to help them fix their credit if needed.

### Understand Credit Issues

One major issue with getting a buyer financed is their credit, because this is what usually keeps a buyer from qualifying for a loan. Therefore, you must learn how to assist your buyer in correcting any credit issues which might prevent them from being able to buy your home.

In fact, most skilled investors are very proficient in the art of credit repair. This is why we have included a bonus chapter in this module on credit repair. You'll need to study that chapter not only for repairing (or strengthening) your own credit, but so you can help your buyers with their credit as well.

## Carrying Second Mortgages

If a buyer has limited credit, they may not qualify for a loan amount sufficient to cover the balance of the purchase price after they put what money they have down.

- For example, if you are selling a house for \$100,000 with the buyer putting down \$5,000 and the buyer only qualifies for an \$80,000 first mortgage ... the buyer will be \$15,000 short.
- **So, to get the deal done, you would have to hold back a seller carried second mortgage for the \$15,000.**

If you're going to be **retailing properties**, there is a good chance you might have to carry back a second mortgage. Therefore, there are some important issues you should know about.

- First, **you should not put a prepayment penalty in your mortgage because you should want the buyer to pay you off early.** It is always better to get your money sooner, than later. So, don't penalize the buyer if they want to pay you off early.
- Any time you take a mortgage back on a property, **make sure the buyer gets a fire insurance policy and names you (the mortgage holder), as "additional loss payee".**
  - This way, if there is any damage to the property or a fire at the property, you know that the insurance company will pay you as a mortgage holder on the property.
  - Also, if the policy is not renewed or is canceled for any reason, you will be notified, at which time you can contact the borrower to make sure the insurance does get maintained.
  - If the borrower does not maintain proper insurance on the property, it is usually standard in all mortgage agreements that you as the mortgage holder can purchase a policy on behalf of the borrower and add it to their mortgage balance.
- You will also want to **make sure that you get a lender's title policy at closing so that you know that your mortgage is properly secured against the property** and
- that your mortgage is protected against any unknown liens or encumbrances.

Finally, **if you want to sell a second mortgage to a note buyer, they usually won't give you much for it, especially if the note has not been "seasoned" for 6-12 months.**



- (By the term "seasoned", we mean how long the buyer has been paying on the note for a period of time.) You can however use these notes as payment to other investors on other deals, or as a down payment to a private seller on another property.

## Lease Options

Another financing technique for selling properties is to sell using a Lease Option.

**This is the only seller financing technique you'll want to use when selling because it gives you the most control over the deal as the seller.**

- You may have bought the property you are selling through any of the creative finance techniques we have covered in this course.
- This includes having bought the property under a Lease Option yourself and you are now looking to **Sub-Lease Option** (second part of the Sandwich Lease Option) the property.
- When selling under a Lease Option, you usually won't be looking so hard for the . tenant-buyer to have good credit, but you will be looking for them to put a sizable amount of money down.

### Giving The Tenant/Buyer Time To Qualify

You'd be surprised how many people out there have a substantial amount of money to put down, but who have trouble qualifying for a bank loan.

There are many reasons why a buyer would have \$5,000 (or even \$10,000) to put down, but not be able to go to the bank and qualify for a loan today. **The most popular reason would be that they had past credit problems, but almost everyone's credit can be cleaned up over time.**

The tenant-buyer may also be **self-employed** and not yet have two years tax returns or they could have a **debt-to-income ratio** problem.

Under a Lease Option, the tenant-buyer would have the time needed for them to clean up any past credit problems and establish new credit.

- They would also have time to increase their income, or to reduce the debts which are affecting there debt-to-income ratio.
- This would allow them to get a purchase loan or refinance loan, down the road.

### Helping Your Tenant-Buyer To Qualify

Selling under a Lease Option is just like retailing a house ... You must understand how to get around any credit issues the tenant-buyer may have and be able to eventually get them qualified for financing.

- When selling under a Lease Option, you won't want to put a tenant-buyer in the property and then leave them to correct any problems they may have on their own.
- You as the seller need to step in and help the tenant-buyer get their credit corrected, so you can eventually get your property sold to them.
- Again, you can use the information and form letters [HERE](#)

### Rent Credits

Along with helping the tenant-buyer with their credit, you can also work with them on building up a larger down payment by giving them a monthly rent credit.

- This is assuming the tenant-buyer did not give you a substantially large deposit on the Lease Option.

**By the way, if the tenant-buyer fails to exercise their option, these rent credits are nonrefundable.**

## Creating A WIN-WIN Situation

You always want to create a win-win deal for everyone by getting a homebuyer into a property at a price and a payment they can afford, while making money yourself.

- However, unless you are planning to give the tenant-buyer long term financing, they should be able to eventually get bank financing if they do everything you tell them to do.
- Therefore, your mortgage broker should be able to say that the tenant-buyer has a chance of getting refinanced in the future, once certain roadblocks have been corrected.
- **Otherwise, you shouldn't let the buyer into the property.**

## Strategies Not To Use When Selling & Why

As a real estate investor, there are several investments techniques which you can use to buy properties, that you won't want to use when selling properties.

### Assigning Sales Agreements

First of all, when dealing in the Wholesale Section, you can either do a double closing to your new buyer as we discussed earlier, or you can assign your sales agreement to the other investor and let them close the deal.

- However, you'll almost never want to assign your sales agreement unless you have collected all the money you're making on the deal upfront.
- This is because if you assign your purchase and sale agreement to another person, you have just given complete control over the deal to them.
- If they don't close like they are supposed to, you won't be collecting your money at closing, because there won't be a closing.

We have included an **Assignment Of Contract agreement** (3.4) just in case the situation calls for it.

- This would usually be when you're only making \$500-\$1000 on the assignment and the new buyer is willing to pay you all of the money upfront.
- This specially designed Assignment Of Contract also allows for you to take a binder deposit and then complete the assignment only once the assignee has made it to closing.
- We'll be covering more about how to properly use this agreement later on.

### Selling "Subject To" On Your Own Property

**Another strategy to avoid when selling is doing a "Subject To" sale on your own property in which you are the borrower on the underlying loan.**

Unless you are extremely motivated to sell, you won't want to hand over the title to your property and trust the buyer to make your mortgage payments for you.

**It is OK, however, to sell using the "Subject To" technique when you bought the property "Subject To" yourself from another seller.**

### Seller Held Mortgages Or Wraps

For the same reasons we just stated, you won't want to sell under a wrap around mortgage either, if you are the borrower on the underlying loan. It is OK though to sell under a wrap mortgage if you took over the property "Subject To".

**You also won't want to give a seller created first mortgage when selling.** It is much better to "test drive" your buyer first by giving them a Lease Option.

This way, you can make sure they'll make the payments like they should, before you hand over the title and take back a mortgage.

- You can simply convert the Lease Option to a seller held mortgage later if you want.
- It is OK, though, to hold "second mortgages" on properties you are selling. This may be especially necessary when dealing in the Retailing Deal Section.

### Contract For Deeds

Finally, you shouldn't sell any of your properties under an Contract For Deed, when you can always structure the deal using a Lease Option.

- Again, by using a Lease Option, you keep more control over the property.
- For instance with a Lease Option, you'll be in a landlord/tenant relationship. Therefore, if the tenant-buyer doesn't pay like they should, all you have to do is evict them.
- Whereas under a Contract For Deed, you would most likely have to foreclose on the property you are selling.
- You would also lose most of your tax benefits by selling under a Contract For Deed.
- There are just too many other benefits as well with Lease Options that you just don't get when selling under a Contract For Deed.
- **So remember, it's OK to buy under an Agreement For Deed, but always sell under a Lease Option.**

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## Hard Money Mortgage Brokers

Probably the most important money source you will use as a real estate investor is a hard money mortgage broker. They are the same as a regular mortgage broker; however, the type of loans they are brokering are very different.

The term "hard money" means a private loan with a high interest rate. These types of loans usually come from a private individual who works with the mortgage broker to loan their money out to real estate investors, and they make it very easy for a real estate investor to buy a property without having to worry about credit requirements or putting money down.

### Hard Money Terms

Most hard money brokers use about the same lending guidelines when it comes to the terms they give on the loans they broker.

## **LTV**

They will usually lend up to between 50% to 65% of the property's "after repaired value". This means they are not concerned with the property's current value, but rather are more concerned with what the property is worth after it is fixed up and the dollar amount it will take to do any necessary repair work.

## **Term**

The term on most hard money loans are between 1 and 2 years. A hard money loan is only meant to be used short term so you can either fix a property up and resell it, or get it refinanced. It is important to remember that if you plan to own the property for 12 months (so that you have 12 months seasoning before refinancing), a 12 month term on your hard money loan is not long enough. This is because you'll be refinancing "after" you have the 12 months seasoning; therefore, you need a term that is at least a little longer than 12 months.

## **Interest Rate**

The interest rates start at about 12% and go up to as high as 18% depending on your local state usury laws. Most hard money loans start at 14%, and 18% is not unusual at all.

## **Interest Only Payments**

To help off set the higher interest rates charged on these types of loans, most lenders allow you to make "interest only" payments. This is beneficial to both you and the lender.

First, you have a lower monthly payment because you don't have to pay any money towards the principal. This keeps your overhead down and allows you to defer paying off any principal until you have made a profit. Besides, if the loan is only for 12 or 24 months, you wouldn't pay much of the principal off anyways.

As for the lender, by not having any of the principal paid off, they keep all of their money invested, allowing them to earn interest on all of their money throughout the term of the loan.

## **Points**

Some brokers also charge between 5 and 10 points upfront on the loan. One point is equal to one percent, so this means between 5% and 10% of the loan amount will be charged upfront at closing. However, there are a lot of brokers and lenders who don't charge any points at all.

## **Prepayment Penalties**

Some brokers also charge a prepayment penalty. This is usually 3 months worth of interest as a penalty for paying off the loan early. The main purpose is to create another profit center for the lender and to make sure they don't just collect one month's interest on the loan if you happen to flip the deal.

Some brokers charge this fee in addition to charging points, while other brokers may not charge any points, but do charge a prepayment penalty.

## **Getting Money For Repairs**

One of the best things about using hard money is that most hard money brokers and lenders will loan you more money than what you are buying the property for. This is because the loan amount is usually based on the property's after repaired value and not your purchase price.

Some hard money lenders will even allow you to borrow more money than what is needed to purchase the property and pay for the repairs. As a beginning investor, this extra money can come in very handy with making the monthly mortgage payments until you get the property fixed up and either sold or rented out.

Any money needed for repairs will usually be set aside in an escrow account with the closing agent. This is important because most of the properties you will buy using a hard money loan, will need work.

As part of the repair escrow, you'll have an escrow schedule which states what work will be done at the property and how much money will be disbursed as each set of repairs is completed.

## **Credit Requirements**

Another great thing about hard money loans is that almost everyone can qualify because the loans are based on the property and not your credit or job history.

Most hard money lenders don't worry about your credit or even check your credit, because they are not very concerned about you making the payments. If you don't make the payments, they will get the property back at a steep discount because the loan-to-value that they lent you was very low. However, some lenders may require a minimum credit score of 600 or 650. A lot depends on the particular brokers lending guidelines, the property, and your rapport with them.

## **Hard Money Is Cheap!**

Now that we have discussed some of the rates and terms associated with hard money loans, you may think that hard money is expensive. However as a real estate investor, hard money is actually a fairly cheap way to go.

If you calculate up what an interest-only payment would be for 18% on \$50,000, the payment is only \$750 dollars a month. Even though 18% may come as a shock to you, as you can see, the payment is not astronomical at all.

Besides it is not the cost of the money that counts, it is the availability of it.

Not having the money needed to do a deal can be very costly if you miss out on the deal all together. In addition, paying a hard money lender as high of an interest rate as 18% (plus points and prepayment penalties) comes out a lot cheaper than paying 50% of your profit to a partner.

Finally, if you are borrowing money for a short period of time, the interest rate you pay will not have any serious impact on your deal, and if the cost of the private funds kills your deal then you are paying too much for the house anyway.

### **Documents Required**

To get a hard money loan, you should be familiar with some of the documents associated with this type of financing ahead of time.

### **Appraisal**

First, is the appraisal. Because almost all hard money loans are based on the property's "after repaired" value, you'll need to get what is called a "Subject To" appraisal. This simply means that the "after repaired value" stated on the appraisal is "subject to" a certain list of repairs being completed. Of course, you'll have to provide the list of repairs to the appraiser ahead of time.

### **Insurance**

Prior to closing, you'll also have to get a hazard insurance policy naming the lender as additionally insured. This protects the lender against loss in the event something should happen to the property.

### **Termite Report**

In addition, you may be required to get a termite report depending on what area of the country you live in. This is to make sure there is not any unseen damages which need to be included as part of the repair escrow.

### **Survey**

Hard money lenders almost never require a survey. However, the title company may require one as part of issuing title insurance.

### **Lender's Title Insurance**

At closing, you will have to purchase a lender's title insurance policy. This policy protects the lender against title defects. However, don't misunderstand and think this policy also protects you as the owner. If you want title insurance for yourself, you'll also have to purchase an owner's policy. Usually, this policy only costs a small extra fee of around \$100 and we highly recommend you purchase it.

### **Note And Mortgage**

The note and mortgage for your loan may be prepared by your mortgage broker or by the closing agent. In either case, you'll want to double check the terms of the agreements to make sure you are getting what you agreed to.

### **Assignment Of Rents**

Another document you'll be presented with at closing is an "Assignment of Rents" form. In the event you default on the loan, this form protects the lender by allowing them to collect any rent payments up to the amount they are owed on the mortgage. This is a standard form most lenders require and it only can be used if you don't make your payments as you have agreed.

### **Escrow Agreement**

Finally, is the repair escrow agreement. This should clearly outline what repairs will be done along with a schedule of draws. A "draw" is a partial disbursement of funds after a certain portion of the repairs have been completed.

Each portion of repairs should be grouped according to the schedule in which they will be performed along with the specific dollar amount to be disbursed after those repairs are completed. It should also clearly state a time frame in which the lender will inspect the property and any fees which may be associated with the inspections or draw disbursements.

To protect both yourself and the lender, any money for repairs should always be set aside in an escrow account with the closing agent.

### **Getting Your Wholesale Buyers Financed**

Hard Money Brokers are not only a great source of easy financing for yourself when buying properties, but they are also great to use for getting your buyers financed when you are dealing in the Wholesaling Quadrant. Knowing how to help your flip buyers get financed helps you to get your properties resold faster. Furthermore, the fact that you can assist the buyer in getting quick financing with money for repairs, can even increase the sales price you can get on the flip.

The key is to know the terms at which the broker will lend money. Then when a buyer calls you on a wholesale deal you are selling, you can tell the investor that if they like the property, you can get them a loan at X amount of dollars at X interest rate and so on. If they are interested, they can give you a deposit and you will then send them to your broker. You can even agree to give them their deposit back, if your broker will not finance them. This way, they have nothing to lose.

Of course, you don't want to send a bunch of buyers to your hard money brokers thus giving away your financing sources. Therefore, you should only refer a buyer after they have signed a sales agreement and given you a deposit. You can also get a non-circumvention agreement from the broker. The agreement should state that the broker agrees

not to lend money to an investor (on other deals) who has received a loan in connection with the purchasing of one of your properties. Hard money brokers understand the competitive world of real estate investing and most do not have a problem with signing such an agreement especially seeing as how you will be sending new borrowers their way.

You should also get a non-circumvention agreement signed if you get one of your private lenders or partners to finance your buyer. In either case, you can have the broker or lender sign an agreement, as well as have the buyer sign a separate copy.

### **Be Careful Who You Bring To Your Sources**

You should also be careful who you take to your hard money sources. If the investor you refer over does not follow through on the investment and the private lender has to take that property back, this can reflect badly on you. You don't want to get a reputation of providing bad borrowers. Otherwise, the hard money lenders will quickly cut you off, even though you aren't the one who defaulted on the loan.

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## **Hard Money Private Lenders**

One way to save yourself from paying brokerage fees to a hard money broker is to find private individuals who will loan you money directly. These may be people who are already loaning money through brokers or they may be new people which are interested in getting started as a lender.

At this point when we use the term "hard money lender", we are talking about the private person who is loaning out their personal money. This is the person a hard money mortgage broker works with to broker their loans. What you want to do is work with private lenders directly the most you can. Not only will you save yourself the fees of a mortgage broker, but you'll many times be able to get better terms. But don't worry about having to pay a mortgage broker; its just another cost of doing business you must factor into your deal until you get your own contacts.

## **Private lenders Are Not Partners**

When dealing with private lenders, you must understand that they are not partners. A private lender is simply someone who lends you money, just as if they were a bank giving you a loan. The lender collects a mortgage payment and does not share in any of the profits from the investment property itself. The private lender's interest is secured by a mortgage (or trust deed) and the lender does not have any ownership in the property's title. Furthermore, the lender has no say-so over the repairs other than your escrow agreement and they also have no control over your sales or rental marketing.

## **Partners Vs. lenders**

If you are giving them a mortgage secured by the property, then they are a lender. In this case, the lender simply makes you a loan and you control the investment property.

If however, the moneyman is putting up the money in exchange for partial control over the investment property and a share of the profits, then they are a partner. In this case, the partner is not given a mortgage but rather their interest is secured as an interest in the actual ownership.

## **Have Multiple Lenders**

You should work on having a diversified set of private lenders. Some private lenders don't want to invest in the junker houses and other private lenders will lend on just about anything they can get a safe return on; therefore, you should have multiple lenders for which to work with. This way, you can select the right private lender depending on the particular investment deal and what the lender is looking to loan against.

## **The Money Circulates**

Once you get enough private lenders, you won't have to worry about running out of private money. Just about the time they are tapped out, one of your other loans will be paying off and you will be able to again borrow that same money. It is like a revolving door where you borrow money and give it back, and then borrow it again. The key is to have several lenders who have enough money to fund all the deals you can get going at one time.

## Finding Private Lenders

We'll cover how to find private lenders and the other money sources who will fund your deals, later on building your team of REI contacts.

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## Working With Partners

As a beginning real estate investor, having a good partner to work with can be of great assistance. Trying to do real estate investing by yourself can be difficult if you have limited funds and want to do a deal that requires out of pocket money. By using the right partners, you can do deals that you otherwise wouldn't be able to do by yourself.

It is very important that you partner with the right people for the right reasons. The key concept behind forming any partnership is so you can undertake a task with someone, that you would not be able to accomplish by yourself. What this means is that your partner should complement your weaknesses.

For instance, if you don't have any cash to invest, your partner should have cash.

## When Not To Partner With Someone

As a beginning real estate investor, you must understand when not to partner, just as much as you must understand when to partner.

### **The Blind Leading The Blind**

If you don't have any cash or experience, don't partner with other people who are in your same boat. This is commonly referred to as "the blind leading the blind". However if you're both trying to get started in this business, there is nothing wrong with studying together and sharing ideas or experiences.

### **Partnering With Friends Or Family**

Also, it is almost never a good idea to partner with friends or family. Business is business and you don't want friendships or love influencing your business decisions.

Partners have disagreements all the time. If things don't work out, they can always go their separate ways, but with friends and loved-ones this is not so easily the case.

### **When You Can Borrow**

One of the key times you should not partner is if you can afford to borrow (or come up with) the money needed for the deal from a private lender or some other source.

Remember, paying a private lender upwards of 18% interest is almost always better than paying your partner 50% of your profit.

### **Long Term Rentals**

Another time to steer clear of using partners is on small rental properties you plan to keep long-term. You just don't want to mix your retirement plans and financial goals with the goals of another person and these types of partnerships almost never work out. Usually, people only partner long-term on larger rental properties of at least four units or more.

## Determining To Partner Or To Borrow

When you have a deal which you are looking at buying, you must decide whether or not you want your moneyman to be a partner, or whether you want them to be a lender. You have to ask yourself...

- "Do I simply want to borrow the money necessary to purchase and rehab a property while being solely responsible for the investment?"
- Or, would I like a partner to put up the money and for me not have to pay monthly mortgage payments? "

**The main determining factor should be whether or not you have the time, skill and financial ability to do the deal on your own.**

You must also identify what your moneyman's objectives are with investing their money.

- Do they simply want to loan you money and get a flat rate of return on a loan" or
- do they want to take an active role in the investment itself in exchange for a cut of the profit.

In the next Section on the Agreements Quadrant, we'll be covering how to properly structure various partnership agreements. We'll also be covering more on how to find partners in the REI Contacts Section.

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## Using Your Or Someone Else's IRA To Buy Real Estate

Before you go out looking for private lenders or partners, you need to understand one of the most powerful ways to get people to loan you money, and that is by showing people how they can loan money to you (or invest with you), using the money they already have invested in their Individual Retirement Account (or IRA for short).

In this section, we'll also discuss how you can invest in real estate using your own IRA account. If you don't have very much money in your IRA account (or if you don't have an IRA account at all), don't worry. We'll not only go over the basics of setting up a new account but we'll also discuss how you can grow your IRA account without ever making a contribution again!

**The reason why most people don't invest in real estate using their IRA account is because they do not know it can be done.** Many People especially don't know that they can invest their IRA funds in private mortgages. Most people think IRA investments are limited to stocks and mutual funds. In fact, many accountants don't understand how an IRA buys real estate or that it can even be done.

## TPAs" And "Self Directing"

IRA accounts are handled by what is called a **"Third Party Administrator"**, which is referred to as a TPA. You're probably already familiar with this term if you have an IRA account. If not, just think of the TPA as being like a bank who has your account.

The key to buying real estate using an IRA is to either setup the IRA account with (or transfer the IRA account to), a TPA who allows you to "self direct" the IRA.

"Self directing" means that you have direct control over the investments that the IRA account makes. The TPA must also allow you to invest the IRA funds in real estate related investments.

We'll discuss more about dealing with your TPA and self directing more after we cover a little more about actually investing in real estate using an IRA account.

## You Don't Need Money In Your IRA To Buy Real Estate!

One of the biggest misconceptions about buying real estate using an IRA account is that you must have large amounts of money in your account. There are people who are aware that they can invest in real estate using their IRA. However, many of these people still don't know that they don't need any money in their IRA account to buy real estate. After all, if you can buy real estate using no money down, so can your IRA! Your IRA could even get cash back at closing.

### **The IRA Must Make A Monetary Investment .**

When having your IRA buy real estate with no money at all, some third party administrators will require that your IRA at least make some type of cash investment in the deal, even if it's only \$100. This is mainly to create a paper trail to show that your IRA actually made an investment. Still, putting 100 bucks down is still close enough to "no money down".

### **Infinitive Returns**

One thing to keep in mind is that you cannot measure the return on your investment if you do not put any money into the deal. This is called an infinitive return and there are no limits on the actual return your IRA can make on its investments.

## Growing Your IRA Without Making Contributions

At some point you may decide you want some of the money you are making as a real estate investor to be put aside long term for your retirement, and investing the profits from just one or two investment deals today can turn into a retirement fund worth a fortune.

Most people's objective is to have a tax deduction from their income every year by making contributions from their income, while at the same time building up a retirement nest egg that is tax deferred. However, you don't have to take money out of your pocket to be able to grow your IRA. In fact, there is no reason to ever have to make another contribution to your IRA. The way to do this is by growing your IRA using the profits it makes from investing in real estate.

Best of all, there is no limit on how much your IRA can make off of its investments, there is only a limit on how much you can contribute per year.

## **Contribution Limits**

Although you shouldn't be having to make contributions to your IRA, here are the IRA contribution limits.

2002 through 2004 \$3,000

2005 through 2007 \$4,000

2008 and after \$5,000

For individuals who have reached the age of 50 before the close of the tax year, the contribution limit is \$500 higher than as stated above.

## **Allowable Investments**

Most people are only familiar with the traditional IRA investment options and are not familiar with nontraditional options. They simply make contributions to their IRA and then have a bank invest their money.

Basically, you are allowed to invest in any investment with your IRA as long as it complies with the law and you are with a Third Party Administrator which allows the particular type of investment. However, for the purposes of this course, we're only going to cover the IRA investment options which are related to real estate investing.

As for allowable real estate investments, your IRA can invest in (or own) just about any type of real estate. You can invest in...

- . Residential real estate
- . Commercial real estate
- . Raw land
- . Tax liens and certificates
- . Real estate judgments
- . Time shares
- . Mobile homes
- . And notes.

(Such notes can be current or in default, and you can lend money by creating new notes, which we'll talk about more in just a minute.)

Finally, your IRA can even do. . .

- . Wholesale flips
- . Retail properties
- . "Subject to" deals
- . Agreement for deeds
- . Lease options
- . Straight options
- . And own rental properties

## **Prohibited Transactions**

There are several types of transactions for which you are prohibited from doing using your IRA.

### **No "Self Dealing"**

First and foremost, you can't do what is called "self dealing". This mainly means you can't do any investments in which you can actually touch your IRA's money. This includes having your IRA buy a property from you or buying a property from your IRA.

In addition, your IRA cannot loan money to you on a property you have a personal interest in any way, shape, or form. By the way, don't try hiding the fact you're borrowing from your IRA by placing the property in a land trust either. If you get caught during an audit, the tax consequences can be harsh.



Also, your IRA cannot buy a property for you to live in, nor can your IRA buy a home for your children or parents. However, you can buy a home for your brothers or sisters. Yes, there really is no logic in this particular guideline and most people are not into buying homes for their relatives anyway.

## Can't Operate As A Business

As a real estate investor, you must be careful not to run your IRA as if it were a business. About 5 or 6 deals is the most you can do a year in your IRA. Otherwise, the IRS could rule that you are running a business through your IRA and you wouldn't be able to tax defer the IRA's income.

To make the most money and grow as much of your investment portfolio tax deferred as possible, you'll want to have your IRA only purchase deals which have the most profit potential. All your other deals would have to be done in a separate entity. If you have a spouse, you could even do another five or six deals in their IRA as well.

## An IRA Cannot Guarantee Debts

Finally, your IRA cannot guarantee a note or a debt. Also, if your IRA takes over the payments of a loan, you yourself cannot personally guarantee the loan, nor can your IRA. In other words, the property can be the only security for the loan. **The reason the IRS has this guideline is so that the only thing you (or your IRA) has at risk is the actual money invested in the particular investment.**

There are some important things you should understand when it comes to you or your IRA guaranteeing a debt.

First, realize that if your IRA purchases a property with the intent to retail it, and at the same time the IRA takes out a private loan, **neither you nor your IRA can guarantee the private loan.** This may be an issue for your private lender or it may not, if the lender is only worried about having the property as security.

Second, if your IRA **Lease Options a property**, it has not yet taken title, nor has it formally assumed the underlying debt. **The IRA would only be making a lease payment.**

Also, if your IRA purchases a property "Subject To" the existing mortgage, **neither you nor your IRA will be guaranteeing the debt.** Not guaranteeing or formally assuming the debt is the whole point behind doing a "Subject To" deal anyway.

It is important to have a TPA who can walk you through the processes and tell you what you can and cannot do.

## Choosing The Right TPA

Whether you plan to invest in real estate using your own IRA, or if you plan to show other people how they can partner or loan money to you using their IRA, you must know how to choose the right Third Party Administrator who allows "self directing". Not only that, the TPA you choose must allow real estate related investments and be able to handle the paperwork that comes with owning such investments. Some companies do allow you to self direct an IRA, but only with certain investments that do not include real estate or mortgage notes. So be sure to get a list of investments the TPA company handles, before dealing with them.

## Transferring To A Self Directed TPA

If you or your new lender currently have an IRA, it should be transferred to another administrator if the current administrator does not allow real estate investments. Different TPAs have different processes for transferring the funds in the IRA account, but it's usually fairly easy and only consists of filling out and signing a few forms. If you're looking for people to invest with you using their IRA account, you'll want to have these forms on hand so you can give them to your prospective lender and assist in transferring their account if needed.

**Transferring an IRA to another TPA is not considered a roll over**, so don't worry. In addition, you can transfer your funds from one TPA to another as many times as you wish, but you are only allowed to do this once in a fiscal twelve-month period.

To transfer the IRA funds, some people actually take all the money out of their existing account and then send the funds to the new TPA. **In this case, you would have 60 days to get the funds to another TPA.**

## Fees

Before transferring an existing IRA to a different TPA, or setting up a new IRA, you should find out what their transfer fees are and make sure they will make payments from the IRA for mortgage payments, property insurance, and other related property expenses. Most TPAs will charge a small set-up fee and a small monthly fee to collect various rent and mortgage payments for an IRA.

## Borrowing Or Lending Money Using An IRA Account

One of the main reasons why IRA accounts are a hot topic among real estate investors is because, not only can you buy real estate or lend money using your own IRA account but you can show other people how they can lend you the money they have in their IRA as well. For this reason, you need to understand how to transfer and manage an IRA account even if you don't have (or plan to have) an IRA account of your own. This will allow you to show other people that you are knowledgeable about investing using their IRA.

## Compound And Grow The IRA Faster

You'll also want to be able to show people how investing their IRA funds in real estate will help them to compound and grow their retirement funds faster.

### For example...

If someone is investing a \$50,000 IRA account at a 7% yield, after 5 years their account would be worth \$71,239.23. However, by investing that same \$50,000 in private mortgages at 15% interest, after 5 years the account would be worth \$105,801.94. That's a \$34,562.71 difference just by investing the same funds they're already investing at a higher yield. This doesn't include the fact that they might be receiving prepayment penalties which could increase the yield to 20% or more per year.

If you take these same numbers and increase the term to 20 years, a 7% yield would make the IRA account worth \$204,541.58, while a 15% yield would have grown to \$993,260.87.

**That's an astounding \$788,719.29 difference** and again, this does not include any prepayment penalties which might have been collected!

## Getting The IRA Funds To The Closing Agent

To create a new loan from a self directed IRA, you'll need to contact the TPA and ask what forms must be submitted in order to get funds transferred to the closing agent of the property.

You must make sure the TPA and closing agent work together so that the loan documents are properly drawn up in the name of the IRA account and that the owner of the IRA does not unknowingly (or inadvertently) violate any **"self dealing" rules**.

Also, all the payments on the loan to the IRA must be made out in the name of the IRA and the funds should never be touched by the IRA's owner.

Most TPAs do charge a small monthly fee for collecting and depositing such payments.

Finally, when the loan is paid off, the name on the payoff check must be in the name of the IRA.

To help avoid any problems, the check should be forwarded directly to the TPA by the closing agent.

For more on how to talk to new lenders about the details of making private loans, **be sure to read the section in the Contacts Section module under the chapter on Private Lenders entitled "Answering A New Lenders Questions"**.

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## Buying Property Using An IRA Account

When having your IRA buy a property, it is very important for you to work with a competent TPA and that you make sure you don't violate any "self dealing" rules.

### Getting The Funds Out Of The IRA To Buy The Property

First, when getting a check from your IRA to purchase a property, the check should always be made out to either your title company or the seller of the property. The TPA can mail the check directly to you as long as your name is not on the check. You can then either give the check to the seller or the title company.

By the way, don't give the seller a personal check of your own to hold until they receive the check from your IRA, nor should you have your IRA reimburse you directly for such a check.

### Titling Property

When buying property using your IRA, you don't buy the property in your name, but rather in the name of your IRA account. The title to the property must transfer directly from the seller to your IRA. Title is not allowed to pass from the seller into your name and then to your IRA.

## Using Land Trusts

For liability reasons, you should not have your IRA take title to a property directly. You should put the property in a trust and have your IRA own the beneficial interest in the trust. In this scenario, the IRA does not own the property, but rather the IRA owns the interest in the trust and the trust owns the property.

If you title the property directly in your IRA's name, your IRA is liable for that property. Even if you have homeowners insurance, if a tenant or someone else were to have a major injury at the property, they could get a judgment against the owner of the property, which would be your IRA. This would mean that everything in your IRA is susceptible to a judgment or lawsuit.

To protect yourself, make sure your TPA is familiar with using land trusts and is able to properly counsel you on using them when buying property with your IRA.

## Selling The IRA's Property

When selling a property that is in your IRA's trust, it is recommended for you to have the closing agent make the proceeds check out in the name of your IRA and send it directly to your TPA. If the closing agent makes the check out to the trustee (which could be your corporation, yourself, or someone you trust), simply endorse the check and send the check to your TPA. Do not cash the check and then forward the funds.

## Buying Discounted Notes

One of the allowable real estate investments we spoke of earlier was mortgage notes. Not only can you create new notes by lending money, but you can also buy existing notes. Many note holders are willing to discount the note they are collecting on so they can have their money today, rather than collecting payments over a period of time. If you have money in your IRA, buying notes at a discount has the potential to make some very high yields.

### For instance...

If you buy a \$50,000.00 thirty year note for \$20,000.00, realize that most mortgages are paid off within four to seven years. This is because most people move on the average of every four to seven years, which in turn means they will sell the property and payoff the mortgage note early. The remaining balance on the note will usually be right around \$48,000.00. Combine this pay-off amount with the payments that you collect and the total amount received would be over \$50,000.00. All for an initial investment of \$20,000.00, and received within a four to seven year period.

## Buying Defaulted Notes

You can also buy defaulted notes and mortgages that people are not making then- payments on. You may ask... "Why would I want to buy a note that is in default?" The answer is. .. "So your IRA can foreclose and get the property which is secured by the note." This is referred to as "buying the property through the back door".

If someone is not making the payments on a note, that note has an extremely low value thus, lowering the amount you will have into the property. To calculate how much you. will be paying for the property by the time the process is done, you simple add the price you're paying for the note, to the court costs and attorney fees for the foreclosure.

### Strategy

You can also build money in your self directed IRA by having your IRA buy real estate with little or no money, fixing the property up, and then having your IRA sell the property for a profit and putting the money in your IRA. You can then use the money you build up in your IRA to buy notes and mortgages, or to make private loans at 14% to 18 % interest.

## Wholesaling Properties With Your IRA

One of the quickest ways to build money in your IRA is to flip properties. You can do this by either agreeing to purchase the property using a standard purchase and sales agreement, or by using a standard option agreement.

As we stated earlier, you don't want to violate any "self dealing" rules. Therefore, make sure everything is done in the name of your IRA, that all deposits or option fees come directly from the IRA, and that all profits from the flip are deposited directly into the IRA account.

## Retailing Properties With Your IRA

IRAs can also be used to buy, fix-up and retail properties. Just like when retailing properties without an IRA, retail deals can be done without requiring any money from your IRA (if you can finance the entire deal using private money or around the existing financing). Do remember though, your IRA needs to have some money invested into the deal, even if it is just a hundred dollars.

## **Can't Guarantee Hard Money Loans**

There is one problem though, which we said earlier. ... neither your IRA nor you, can guarantee any loan your IRA gets from a private lender. Therefore, the lender must be willing to use the property as the sole source of security. Sometimes this will-be a problem, and sometimes it won't. It really just depends on what the particular lender's guidelines are.

## **Paying For Repairs**

If you need to do repairs on a property, or otherwise have expenses on a property while it is owned by your IRA, you can have your TPA issue a check from your IRA for the expenses. It is OK to spend money out of your pocket for repairs and then get reimbursed from your IRA later.

## **Lease Optioning Properties With Your IRA**

Your IRA can even Lease Option and Sub-Lease Option properties. As with all agreements on properties owned by your IRA, the IRA should be named as the optionee or optionor.

## **Option Fees**

When Lease Optioning properties, it is very easy to get into properties without having to put any money down; however, as with all investments your IRA makes, your IRA should have money invested to make the deal a legitimate investment. So, when Lease Optioning a property with your IRA, you should at least put down a hundred dollars (directly from the IRA to the seller), as an option fee.

## **Sub-Lease Options**

If you Sub-Lease Option a property your IRA either owns or is Lease Optioning from a seller, make sure all the payments that come in from the tenant/buyer are made out to your IRA.

## **Rental Properties In Your IRA Account**

Just like with Sub-Lease Options, the rent payments should be made out directly to your IRA account. Some TPAs will even collect the rent payment on the property and make any underlying mortgage payments for your IRA.

However, having rental properties in your IRA long term (such as more than a year) could trigger the IRS treating the transaction as a business transaction, which could have severe tax consequences. Therefore, you should only put properties in your IRA you plan to own for less than a year. This means you probably won't be owning any rental properties in your IRA, which brings us to our next topic, which is when not to buy property in your IRA.

## **When Not To Buy Property In Your IRA**

### **Investments Longer Than A Year**

As we just said, you should not have your IRA do deals which would take more than a year. This would usually be rental properties and Lease Option deals to tenant/buyers who most likely would not be able to qualify for a refinance within a year.

### **Limit On Number Of Deals**

One of the things we also said earlier was to avoid doing too many deals using your IRA; otherwise, your IRA could be classified as a business. Doing five or six deals a year with your IRA account shouldn't be a problem.

### **When You Want The Profit Now**

Finally, if you need the money your investments are making now, then don't structure your deals so that your money goes into your IRA.

If you have your IRA purchasing and selling deals, and you keep turning right around and pulling the money back out of your IRA, you'll be defeating the purpose of why you put the money in there to begin with. The whole point of putting money in your IRA is so you can build a retirement account either tax free or tax deferred.

If you want the money so you can spend it, don't have your IRA do the deal to begin with. You would have to pay income tax on the money you take out before you are 59 1/2 years old and there is also a ten percent penalty, and if you have a Roth IRA, you can't take money out, within five years without getting hit with penalties.

## **Opening An IRA Account**

If you don't already have an IRA account, opening one is easy. You can open an IRA account with as little as a couple of hundred dollars and there are no age restrictions on how old you have to be.

The first thing you have to decide is what type of IRA account you want to open. While there are several types of IRA accounts, the two most popular types of accounts are a Traditional IRA and a Roth IRA.

These two types of IRA accounts have many differences, but there are few specific differences we should discuss.

## A Traditional IRA Vs A Roth IRA

The first difference is that contributions to a Traditional IRA are tax deductible and the contributions you make to a Roth IRA are not. This particular difference should not matter much as a real estate investor, because you can grow your IRA without making contributions. If you do plan to make contributions and are looking for the tax deduction, this would be a factor to consider when deciding on the type of account you want.

The main difference you should consider is the fact that while contributions to a Roth IRA are not tax deductible, the money in the account can be taken out "tax free" after age 59 1/2. This means your Roth IRA could make money by investing in real estate and never have to pay tax. This means the money in the Roth IRA can compound "tax free" as well.

On the other hand, while you do get a tax deduction for contributions to a Traditional IRA, the money only compounds "tax deferred". This means you would have to pay tax on your distributions after age 59 1/2. For this reason, if you do not plan on making regular contributions (or are not looking for the contribution tax deduction), a Roth IRA is a better choice for you as a real estate investor.

There are some other important items you should know about.

**First, with both a Traditional IRA and a Roth IRA, there is a 10% penalty** if you withdraw funds prior to age 59 1/2. If you have a Roth IRA, you also can not take any money out within the first five years without paying a penalty (even if you happen to turn 59 1/2 within that period).

Finally, **with a Roth IRA, you're never required to take a distribution**, while **with a Traditional IRA you're required to take distributions after age 70 1/2**.

In addition, **with a Roth IRA your children can inherit the account income tax free**, where as **with a Traditional IRA they can not**.

## Income Requirements

To qualify for an IRA, you must have taxable income and your adjusted gross income for you and your spouse must be under \$160,000. If you are single, you must make under \$110,000.

You don't have to be within these income guidelines every year. All you need is to be within the income guidelines one year, at which point you can open the IRA. If later you make so much money as a real estate investor that you exceed the income guidelines, it only means you won't be able to make any contributions to your IRA account.

## Having Two IRA Accounts

If you already have a Traditional IRA and you decide you want a Roth IRA, you can have both, because there is no rule against having two IRA accounts at the same time. So, if you don't want to pay the taxes or penalties to transfer to a Roth IRA, you can simply open up a Roth IRA in addition to your regular IRA.

## If You Have A 401 (k)

If you have a 401(k) with your employer, you can ask your employer to move your 401(k) funds into a self directed IRA. There is no penalty to transfer funds from your 401 (k) to your IRA or Roth IRA, but you may not be able to move the funds in your 401(k) if your employer will not allow it.

## Individual 401(k)

Another type of account you may want to look into is an Individual 401(k) plan. This plan is very similar to a 401(k) but is complex and is specifically designed for small businesses with few (or even no) employees.

## Who Can Set Up An Account For You

Once you have decided on the type of account you want to setup, you can open an account through a bank, mutual fund company, trust company, securities company, or an accountant.

Make sure the company you choose allows you to "self direct" and allows real estate type investments. They should also be able to answer any remaining questions you may have to make sure you are making the correct decision in regards to your personal situation and objectives.

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## Credit Cards & Lines Of Credit

One final source of money we're going to discuss is credit cards and lines of credit. Some of these credit sources include bank credit cards, home improvement store credit cards, home equity lines of credit, and even signature loans.

### Supplementing Your Other Financing Sources

Credit cards and other lines of credit should be used to supplement your other financing sources. For instance, if you have a lender who will only give you 60% of the "after repaired value" on a property, and you need 70% to get the deal done, you can use credit cards or other lines of credit to make up the shortage. After the house is either sold or refinanced, you can pay the credit bill off with your sales proceeds.

Credit lines also come in great when you don't have the cash on hand to pay for down payments, repair costs, monthly payments while you're trying to retail a property, and so on.

Some people have even used credit cards to finance the entire purchase of an investment property short-term. However, most people do not have the necessary credit limits on their credit cards to pull this off. Besides, it would probably be cheaper to use a hard money lender.

### Bank Credit Cards

Credit cards are a good source of quick funds when you need it most. If you already have one or more bank credit cards, then great; try having your credit limits increased and try applying for other cards as well. If you don't yet have a bank credit card, apply for one the first chance you get.

Do not cringe at paying 20+% on a credit card if borrowing the money means the difference in making several thousand dollars (or more) on a deal. It's just one of those costs of doing business.

### Home Improvement Center Credit Cards

One type of credit card every real estate investor should have is a credit card from each of the major home improvement stores. The reason for this is obvious.

Anytime you're rehabbing a property, these credit cards can come in very handy in helping to pay for cost overruns or repair costs you couldn't finance any other way.

Some stores even offer no interest or no payments on larger purchases when you open a new account. And when applying, don't forget to see if you can get a contractor's discount. Most home improvement centers will give a 10% discount in an effort to get your business.

### Home Equity Lines Of Credit (HELOC Loans)

If you own a home and have equity, you may want to consider getting a home equity line of credit, if you don't already have one. Some banks will give you a home equity line of 100% or more of your home's value. Many banks will even pay the closing costs and the interest you pay may be tax deductible.

If you have a large enough credit limit, a home equity credit line can be a great source of temporary funds for purchasing an investment until you can wholesale it, retail it, or refinance it. Even if you only have a credit line of a few thousand dollars, that money can still come in very handy if needed.

You should take extra care and make sure you use your home equity line wisely. You don't want to put your personal home at any unnecessary risk. So, only use this money to invest if you know the deal is a sure thing.

### Signature Loans

If you have excellent credit, you may be able to get a signature loan or line of credit. As with the other credit sources we've just discussed, it's good to have a supplemental source of money just in case you come across a deal that requires it.

### Using Co-Signers

If you can't qualify for any of these credit sources, you may be able to get your partner, friend, or family member to co-sign with you as part of the deal. Be sure your name is on the account so that the account can help to build up your credit to where you can qualify on your own later.

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## Bonus Chapter Credit Repair

# Credit Repair For Real Estate Investors

In this bonus section, we'll be covering some of the basics of credit reports and credit repair. Although the full discussion of credit reports is beyond the scope of this course, it is important that every real estate investor have at least a basic understanding of how to obtain and read a credit report, as well as be able to do simple credit disputes and repairs.

This credit report knowledge is not only useful when dealing with your own credit, but it is very helpful when dealing with potential buyers and their credit.

## Your Personal Credit

One of the main purposes of this course is for you to learn how to invest in real estate using no money and no credit. However, as we have already discussed, there are situations when having good credit can make or break a deal. Also, having good credit increases your financing options, which in turn opens more doors to more investment opportunities.

## Know Your Credit Condition

It is important to learn about your current credit situation so you can establish any limitations you may have on getting new financing. The best way to do this is to sit down with an experienced mortgage broker and go over your credit report. They'll be able to point out problem areas which need to be addressed and they'll tell you what loan programs you should be able to qualify for.

## If You Have Bad Credit

If you have bad credit it is important to realize that you are not alone. All over the country, millions of hard working and honest people fall into hardship every day. The good news is that no credit is so bad that it can't be repaired over time. In addition, you have legal rights to protect yourself when dealing with your credit and you can repair most errors or discrepancies by yourself.

## Credit Errors Can Cost You Deals

Even if you know you have good credit, you still need to request a copy of your credit report and make sure there are no discrepancies or mistakes on it.

You don't want to make a loan application and then find out there is an error which will hold up your loan approval. Some errors may take several weeks to resolve. In the mean time, your loan being held up could cost you a deal.

If you have not paid particular attention to your credit, then now is the time to do so. In this bonus chapter, you'll learn how to get a copy of your credit report, how to dispute any errors on your credit report, and how to rebuild or expand your current credit.

## Your Buyer's Credit

The information in the bonus chapter is also very useful when working with buyers who will be getting conventional financing. By knowing how to correct minor credit problems and how to use alternative credit references, you'll be able to sell properties to buyers who might not have been able to qualify for a purchase loan otherwise.

Your knowledge of credit will also help you to better pre-qualify buyers over the phone and it will help you to more effectively deal with a buyer's loan processor. If you plan to sell properties under a Lease Option, knowing about basic credit repair will be especially important. After all, the lease period is the time which the tenant/buyer should be using to build up their down payment as well as their credit. Investors who are successful at selling under a Lease Option all have a good working knowledge of how to work with a tenant/buyer on any credit problems which are preventing them from getting a loan.

## Understanding Your Credit Report

### Getting A Copy Of Your Credit Report

The first step to working on your credit is obviously to get a copy of your credit report.

#### Getting A Free Copy Of Your Credit Report

If for any reason you have been denied credit within the last thirty days, you can request a free copy of your credit report. When you receive a credit denial letter, it should list the credit bureau which provided your credit file. Under the Fair Credit Reporting Act, this bureau is required to provide you with a free copy of the credit file they maintain on you, seeing as how you were denied credit based on their file.

If you have not been denied credit in the past thirty days, the credit bureau will supply your credit report to you for a nominal fee, which we'll talk about in just a minute.

### **There Are Three Main Repositories**

There are three main repositories. They are Experian, Equifax and TransUnion. Every credit report is created using data from one of these bureaus or a combination of data from two of them, or all three.

### **Ordering Online**

All three of these credit bureaus offer online credit reports. This can give you instant access to your credit files.

### **Ordering Over The Phone**

You can also order your credit report over the phone.

### **Ordering By Mail**

If you don't have internet access, or don't have a credit card for ordering over the phone, you can mail a money order with a written request for a copy of your report. It is best if you call the credit bureau ahead of time to make sure what their current fees are.

- \* First, middle, and last name (including Jr., Sr., III, etc.)
- \* Current address
- \* Previous addresses for the past two years, if any.
- \* Social security number
- \* Date of birth
- \* Current employer
- \* Phone number
- \* Signature
- \* And credit report fee

The following information about yourself should be included as part of your written request. ..

A sample request letter has been included for you (2.1).

### **Credit Bureau Contact Information**

#### **Experian**

P.O. Box 9595 Allen, TX 75013-0036 888-397-3742 [www.Experian.com](http://www.Experian.com)

#### **Equifax**

P.O. Box 740241 Atlanta, GA 30374 1-800-685-1111 [www.Equifax.com](http://www.Equifax.com)

**TransUnion Consumer Disclosure Center** P.O. Box 1000 Chester, PA 19022 800-888-4213 [www.TransUnion.com](http://www.TransUnion.com)

## **Check All Three Repositories**

It is very important that you get a copy of your credit report from each of the three credit repositories. Each one of those repositories contain information about your credit and while they do share information, many times there will be a record in one repository that is not in another. It is as if you actually have three different credit reports.

So if you request your credit report from only one of the three repositories, the repositories you did not request a credit report from may contain negative information you need to dispute.

### **3-in-1 Credit Reports**

All three of the main repositories do offer 3-in-1 credit reports. These credit reports contain all the information in your credit file for all three repositories. For the most accurate picture of what your credit files look like, we recommend that you get one of these "combined" credit reports.

### **Contents Of A Credit Report**

When it comes to reading a credit report, all three of the main credit bureaus have their own layout and information code system. In the past few years, they have tried to make their credit reports clearer so people can understand them more easily.

All three bureaus do report the same types of information in their reports though. This information includes the following ...

### **Basic Information**

Basic information such as your name, address, date of birth, social security number



and spouse's name.

### **Credit History**

Credit history information listing companies that have loaned you money in the past, along with the account numbers, size of your credit lines, dates the lines were opened, dates you last used the credit lines, repayment terms, amounts you presently owe, status of your payments and number of months your payments are past due.

### **Collection Agencies**

They also maintain information on any collection agencies who are assigned to collecting an overdue debt you owe, along with the original creditor's name, the amount it tried to collect, and whether you paid.

### **Additional History Information**

Finally, some of the additional information they maintain includes your former addresses, and current (and former) employers.

### **Courthouse Records**

In addition, the credit bureaus also maintain information from courthouse records including federal, state or local liens, bankruptcy filings and other judgments.

### **Inquiries**

A list of inquiries made by potential credit grantors (like credit card companies), is maintained as well.

### **Things That Affect Your Credit Score**

One of the most important aspects of your credit report, is your credit score. All three bureaus do create their own credit score for your file, and because each of the repositories use different guidelines for scoring your credit, your credit score will be different at each one.

A credit score is based on a model derived from analyzing the past credit history of thousands of people. Based on the collective credit history of thousands of people with a financial profile similar to yours, the credit score tries to estimate your future behavior in respect to repayment of your loans, making timely payments, etc.

Some of the factors considered when determining your credit score include the following ...

### **Payment History**

First, is obviously your payment history. If you don't pay your bills on time, you are clearly more of a credit risk and your credit score will be lowered.

### **Amounts Owed**

How much you owe to your creditors is also a factor. This not only includes how many of your accounts have balances, but how much of each credit line is in use. For instance, if you have a \$5000 available line on your credit card and you owe \$4800, this will pull your credit score down, whereas if you only owed a couple of hundred dollars, you would have a higher credit score.

### **Length Of Credit History**

The length-of your credit history is very important. The longer your accounts have been open, the more it shows that you can handle long term financial obligations.

### **Types Of Credit In Use**

The types of credit you have qualified for play a factor in your score as well. For instance, having a department store credit card is not as valuable as a major credit card or home loan.

### **Are You Taking On More Credit**

If you take on a lot of new accounts within a short period of time, this will also reduce your credit score. New debt is not helpful to your credit report mainly because you haven't had time to create a payment history on the accounts.

Shopping for new credit is just as bad. Many people who are having a tight time with their finances will begin looking for new credit. If you do find the need to apply for credit at several locations, try to do the applications within a fourteen day period. This will help to keep the credit inquiries from affecting your score.

### **Unused Credit Affects Your Score**

Even unused credit can affect your score in a negative way. If you have numerous open accounts that have zero balances, you still have the ability to access those accounts. While having a couple of unused accounts may not pose a problem, having

too much available credit can.

### Disputing Things Off Your Credit

Once you get a copy of your credit report, there are two ways in which to make repairs. The first way is to dispute any incorrect information which your credit report contains. The second way is to payoff any outstanding debts you may owe.

If you have previously made late payments, the only way they can be removed is by either disputing the fact that you were late, or by waiting until the item is so old that it drops off your credit report (this is usually seven years).

In this module, we have included several sample letters for you to use when disputing items on your credit with the credit bureau who is maintaining your credit file.

### Disputing Inaccuracies

If you find that your report has inaccurate information, you can dispute the information and the credit bureau has to investigate it within 30 days. Until the disputed item is proven to be accurate by the creditor, the credit bureau cannot put the disputed information on the credit report unless they include your written statement of dispute.

If you prove that the information is inaccurate, then the information has to be removed from the report permanently within 30 days. A sample letter for disputing inaccurate information is included in Exhibit 2.2.

### Information To Include With Your Dispute

Some of the information you should include in your dispute letter would be the full company name associated with the disputed item, the account number, and reason for your dispute (such as, it is not your account, you have paid the account, etc.)

### Incorrect Information In Your Favor

By the way, if there is any positive miss-information about you or information that is good but not yours personally, don't try to remove or correct it. Even though the information may be incorrect or about someone else, it is on your credit report and helping you.

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### Dispute Statements

You can also request that a statement be included in your file. Most credit bureaus allow both the consumer and the creditor to make statements to report what happened, if there is a dispute about something on the report.

### Removing Old Information

Credit reports normally only contain information that is less than seven years old, with bankruptcies remaining for ten years. Anything older than that should have automatically dropped off. If not, you should send the credit bureau a letter similar to the one (2.3).

### Remove Unauthorized Inquiries

You should also request that any inquiries which you did not authorize be removed as well. Anyone who requested a copy of your credit report should have had your permission ahead of time.

### Remove Spouse's Information

You can also request that derogatory account information regarding your spouse be removed from your credit report, if you are not liable on the account.

### Follow Up After 30 Days

As we said earlier, the credit bureau has thirty days to investigate your dispute or request. If after this amount of time you haven't heard back, call the customer service department. There is usually a toll-free number on the credit report you can call for assistance or you can send the credit bureau a letter using the example in Exhibit 2.6. If you call on the phone, remember to keep notes of who you talked to and on what dates.

### Re-review Your Credit Report

When you do finally get a written response from the credit bureau, by law you should also receive a new copy of your credit report (if there were any changes). You'll want to double check for the changes you had requested, to make sure your credit report is now accurate.

Once any information is changed on the report, the credit bureau cannot change it back unless the creditor provides proof that it was accurate. In this case, you'll get notification from the credit bureau that the item has been put back on your report.

#### Paying Things Off Your Credit

If you owe money to a creditor, and you cannot dispute the item off of your credit report, the only other way to get it off is to pay it off.

There are two ways you can payoff any bad debts you owe ... One way is to payoff the balance with a lump-sum payment (hopefully at a discount). The other way is to payoff the account by making installment payments over a period of time.

#### Dealing With Charge Offs

Some of your past due bills may have become what is referred to as a "charge off". This means that the creditor has either turned your past due account over to a collection service or has otherwise written the account off as a loss. As a result, the account balance shows as an unpaid and overdue balance on your credit. This is very harmful for you if you try to qualify for new credit somewhere else.

#### When To Deal With Charge Off Accounts

The time to deal with creditors on charge off accounts is when you either are able to make one large lump sum payoff or make monthly payments on a regular basis.

#### Paying Off Overdue Accounts In A Lump-Sum

If you decide you want to payoff an account in one lump-sum payment, you should always try to get a discount on the amount you owe.

Furthermore, you're going to request that the creditor remove all negative information on your credit file. Some creditors will not report the payments as on time, but instead will report the charge account as "non-evaluated", rather than "past due" or as a "charge off".

If you want to payoff a debt at a discount, call or write the creditor and let them know that you can't afford to pay the full amount; however, you would at least like to pay off the majority of the account. It is not unusual for creditors to accept 60% or even 50% as payment in full. Simply start by explaining to them your financial condition. Of course, make things look as though they are not getting better, but that you are still credit conscious.

#### A Discounted Payoff May Get You A 1099

It is important to know that if you payoff a debt to a creditor and the creditor forgives a part of the debt equal to \$600 or more, they must send you an IRS form 1099-C at the end of the tax year. This means that when you file your tax return, you must claim the discount as income because of the fact that it was forgiven by the creditor.

The only exceptions to this are ... that you were no longer required to pay the debt because the collection time had expired ... the amount discounted was for late fees, interest or any other charge that was not part of the original principal of the debt. ... or you discharged or eliminated the debt in bankruptcy.

#### Always Get A Signed Release

If you settle on a payoff amount less than the full amount owed, be sure to get the creditor to sign a release stating that they are accepting partial payment of the debt and that it is accepted as full payment. You'll also want to get them to agree ahead of time to report the account as either "paid as agreed" or "non-evaluated". A release is included at the end of the sample letter (2.12).

You should also put a statement on the front and back of your check stating that "Cashing this check constitutes payment in full of this account".

#### Making Monthly Payments As Payoff

If you can't make a lump-sum payment, your other option is to make monthly installment payments on the debt. Many creditors will settle for a lesser dollar amount when you pay them in a lump sum; however, most creditors will insist on 100% payment of the debt if you pay in monthly payments.

You will want to either call (or write) the creditor and let them know that you had bad financial problems in the past, but you can now afford to make payments.

#### Removing The Past Due Notation

If you get the creditor to agree, have them remove the "past due" notation on the credit file. But realize, as soon as you miss a payment under your new agreement, the creditor will most likely put the past due notation back on your credit file.

If the creditor won't remove the past due notation on your credit file, get back with them in a couple of months after you have made a few payments. State to them that the negative mark on your credit is keeping you from buying a home, getting other credit cards, and so on. Most creditors will remove the derogatory reference if it is keeping you from getting a home loan, so a letter from your mortgage broker would be especially helpful.

#### Re-aging The Account

In return for making monthly payments on the account, you're also going to request that the creditor "re-age" your account. In other words, the current month will show on your credit report as being the first month of the debt being due. It will be as if the account is brand new and as long as you make the payments on time, the account will show as current.

Sometimes the creditor will not re-age the account until you have made at least 2 or 3 consecutive payments on time. This is OK. Just remember to get everything in writing ahead of time.

#### Things To Know When Negotiating

Here are some things you should know when negotiating about payment of your debts.

#### Business Is Business

First, understand that the person who works for a collection agency or creditor is not your friend. He or she may try to build confidence with you regarding your personal problems or show concern for you possibly ruining your credit. Don't believe them. These people have no concern for your well being. Their only concern is to get you to send them money.

#### Negotiate With The Creditor First

Second, always try negotiating with the creditor before negotiating with the collection agency. The creditor will usually be more likely to negotiate seeing as how they are the one who is actually owed the money. On the other hand, if the creditor sold the debt to a collection agency, the collection agency will be the one who you will have to deal with.

#### Negotiate In Writing

When ever you negotiate, always do it in writing. If you do negotiate with someone over the phone, keep good notes regarding the date, who you spoke with, and what was said. Then have them confirm your discussion in writing.

You must have proof of any agreement you and the creditor come to, and you should always get everything in writing before sending any money.

#### How To Send Letters

Here are some important notes you should keep in mind when sending out letters to a creditor or collection service ...

1. First, type your letters or write them very neatly.
2. Keep a copy for yourself.
3. When sending money, use a cashiers check or money order. This way, if you have other debts in collection, the collection agency won't know your checking account number and be able to pass it on to another debt collector.
4. If you're paying off a debt at a discount, always include a statement on the check that "Cashing this check constitutes payment in full of this account".
5. Finally, always send your letter by certified mail and request a return receipt.

#### Negotiation May Take Time

Sometimes the negotiations on an account can take several weeks. So, don't expect to be able to clean up your bad debts within a couple of days. It's better to take your time and make sure that as much of the derogatory information as possible is removed from your file.

#### What If The Creditor Rejects My Offer?

If you are not able to reach an agreement which you can afford, tell the creditor that it will not work for you and to call you back if they decide to agree with your figures.

If your offer is completely rejected by the person you are dealing with, make sure that you speak with the supervisor. You can also try again a month or so later.

#### Past Bankruptcies

If you have a past bankruptcy, don't worry. You can still get a mortgage loan to buy a property, sometimes as soon as one day after the bankruptcy has been discharge. Of course, these loans come with a substantially higher interest rate and they are even harder to qualify for if the loan is on a non-owner occupied property. In addition, most lenders look for you to have absolutely perfect credit since the bankruptcy and for you to be able to show that you have attempted to reestablish your credit.

There is no way to dispute or otherwise have a bankruptcy removed from your credit report. Bankruptcies stay on your credit report for ten years before they drop off. So, the only way to deal with a past bankruptcy is to work on slowly establishing new credit.

### Defaulted Student Loans

If you have defaulted on a student loan, the government has what is called a "reasonable and affordable payment program". You and the agency holding your loan decide what is affordable for you based on your income and expenses, and come up with a new monthly payment (even if you have already been sued and there is a judgment against you). As long as you make 6 consecutive monthly payments you will be eligible for a new student loan if you want to return to school. After making 12 consecutive monthly payments the agency holding your loan can remove the default notation from your credit record.

### Canceling A Student Loan

You may be able to cancel a federal student loan all together if you qualify under one of the following situations ...

You co-signed for a student who dies, you become totally or permanently disabled, you served in the US military, you're a school teacher serving low income students, or a teacher designated in a teacher shortage area, you are a full-time nurse or a medical technician, you're a full-time law enforcement or corrections officer, you're a fulltime worker in a head start program, peace corps or VISTA volunteer, your school falsely certified that you were eligible for a student loan, or the school closed before you completed your program of study.

If you qualify under one of the situations we just stated, you'll want to contact the Department of Education's Debt Collection Service.

## Building Stronger Credit

Once you have attempted to dispute or payoff any bad items on your credit report, the next step is to work on building your credit report up with positive credit references. This can be done by adding credit references you already have but aren't getting reported, and by establishing new credit references.

### Strengthening Your Current Credit References

One way to build stronger credit is to try and strengthen the credit references you already have.

#### Increase Your Credit Limits

If you already have a credit card with a low credit limit, ask the creditor to increase it.

Having a major credit card with a substantial credit limit can be very beneficial to your credit score, as long as you keep the account in good standing.

### No Credit Is Good Credit

If you are starting off with no credit at all, it's important to understand that having no credit is better than having bad credit because your credit report is like a clean slate.

If a potential buyer (or lease option tenant) says they don't have any credit, they are good candidates because of the fact that their credit is not bad. As a real estate investor, all you have to do is work with them to beef-up their credit a little bit. Before you know it, they're sitting there with a loan approval to buy your house.

### Adding Information To Your Credit Report

The next thing you should do to help build up your or your buyer's credit, is to add credit references to your credit report which are not currently being reported.

### Spouse's Information

One source for credit references can come from a spouse. If your spouse has good payment histories on some current credit lines, have your name added to the account and then have the account added to your credit report.

If you are already on your spouse's account, but the account does not show on your credit report, you should request that the creditor begin reporting the account in both your names. This is of course assuming that the account is in good standing and has a history of being paid on time.

A sample letter for requesting that a creditor beginning reporting information in both spouse's name (2.6)

You can also have your name added to your parent's credit card account (assuming your parents have good credit). Your parents don't even have to give you a card. Just having your name on the account, is all you need. The credit history of the account will show on your credit report and give you an instant credit history boosting your credit score.

### Unreported Credit

You should also check your credit report to see if there are any accounts that you are paying on which are not getting reported to the credit bureau. If you find one, contact the creditor and request that they begin reporting your

information. If the creditor does not (or will not) report to the credit bureau, an alternative you have is to get the information added as part of a "full factual" credit report.

#### "Full Factual" Credit Reports

A full factual credit report is just what its name says, it contains a full set of facts. For an extra fee, a credit bureau will call up a creditor to verify the credit history and then add the information to your credit file. They will also call to verify other information within a short period of time and then update the credit report accordingly.

This is a quick way of getting information added or removed from a credit report. This type of service is mainly used by mortgage brokers who need to get a borrower's credit file updated quickly so that the borrower can qualify for a loan. It is also a great way to get alternative credit added to the report when the borrower does not have enough credit references.

#### Adding Alternative Credit

Alternative credit references which you could add to your credit report (or your buyer's credit report), include some of the following ...

- \* Electric and water bill payments
- \* Phone bill payments
- \* Unreported car payments
- \* Insurance payments
- \* Various rental payments
- \* Or any other bill you or your buyer pays on a regular basis.

Usually, a mortgage lender will look for a borrower to have at least three credit references. This is something to keep in mind if your credit is weak. Also, if you are pre-qualifying a retail buyer (or lease option buyer) over the telephone who says they have weak credit, you'll want to ask about any alternative credit references they may have.

#### Credit Report Rescoring

It is important that the credit bureau who is updating your (or your buyer's) credit report do what is called "rescoring", which means that the credit score will be updated once the new credit references have been added. This is important because the credit score can affect a borrower's ability to get a loan approval or a better interest rate.

#### Establishing New Credit

Establishing new credit is a very important step if you have had past credit problems or a bankruptcy.

#### Secured Credit Cards

If you have no credit at all or really bad credit, the first step will be to get a secured credit card. With this type of credit card, you deposit in an account let's say ... \$500. In exchange, the bank will issue you a credit card with a credit limit of \$500 that is secured by the \$500 you have deposited in the bank.

After making a charge on the credit card, you still have to make a payment to pay the balance off. This type of credit card is not a check card connected to the \$500 deposit you made. The deposit you made ahead of time for \$500 is only security for the bank in case you fail to make the payments as agreed.

After paying on time for six months to a year, you can go back to the bank and request that the card be unsecured, and that you get your \$500 deposit back. You can then make requests every six months or so that your credit limit be increased.

#### Good Credit Can Always Look Better

If you already have pretty good credit, qualifying for new unsecured credit shouldn't be much of a problem. Just remember, even if you already have good credit, you should always work to make your credit even stronger and work to get your credit score even higher.

#### Avoiding Future Credit Problems

The final step to building stronger credit is to stay out of trouble and try to avoid future credit problems.

#### Making A Budget

If you tend to have money problems, start by preparing yourself a budget. Write down all your income sources and then write down every expense that you have each month. (even the little things). Compare them and see if you are overspending, then look for ways you can cut back on your spending.

If you have trouble putting your budget together, you can get help from a nonprofit group such as the Consumer Credit Counseling Service, which can help you for free or at a very discounted cost.

#### Paying Your Bills On Time

If you have a bad habit of not paying your bills on time (even when you do have money), set up your monthly payments to be automatically withdrawn from your checking account. This way, you'll never have a late payment, which saves you from paying unnecessary late fees and it helps to keep your credit looking clean.

#### Get Overdraft Protection

Having overdraft protection on your checking account is also very important. When applying for a mortgage loan, the lender will usually request your last three month's bank statements. One of the main things they will look for is whether or not you have had any bounced checks. If so, it is an indication that you are having money troubles or just aren't paying enough attention to your finances.

By having overdraft protection, it helps to avoid any future mortgage application problems. It also helps to save you unnecessary bounced check fees.

#### Avoid Future Financial Problems

Of course, always try to avoid future financial problems. Here are a few things that will help:

- \* Create a realistic budget and stick to it.
- \* Avoid large house or apartment payments.
- \* Charge for items only when you cannot afford it and it is important that you buy it now.
- \* Don't buy on impulse.
- \* Avoid co-signing or guaranteeing a loan for someone.
- \* And avoid joint accounts with someone who has bad spending habits.

As soon as you see you're going to have a financial problem, you'll need to contact all your creditors and let them know you may have trouble paying your bills at that time. What you want to negotiate with them is two things ... one is the time for you to get back on your feet so you can pay, and two ... you don't want any bad credit information reported to the credit bureau on the account.

#### I Can't Pay My Credit Card Payments!

If you feel you can't pay your credit card or other charge account balance, contact the creditor and let them know of your situation. A lot of times you can have a creditor freeze your credit line and allow you to pay a smaller payment each month. Some creditors will even stop the addition of future interest charges, but few will remove any interest charges that have already accumulated.

In addition, ask the charge company to report your payments to the credit bureau as "on time" while you payoff your balance. As long as you keep to your new payment schedule as agreed, the creditor should not report the debt as past due and they usually don't report the special payment arrangements to the credit bureaus.

#### Excuses Creditors Find Acceptable

When talking to the creditor, start by explaining your problem clearly and let them know the problem will be correcting itself in the future. Here are some excuses as to why you cannot pay your bills that creditors usually find acceptable:

- \* Job layoff or relocation.
- \* Pay cut or cut in hours .
- \* Divorce or separation and your ex-spouse fails to pay their part of the bills even if ordered by court order.
- \* Inadequate medical insurance after a major illness or accident.
- \* Permanent or temporary disability which may include heart attack, stroke, cancer and sometimes a less severe illness.
- \* And finally ... large unexpected tax assessments.

## Letters To Credit Bureaus

## Bonus Chapter Credit Repair

### Credit Repair For Real Estate Investors

In this bonus section, we'll be covering some of the basics of credit reports and credit repair. Although the full discussion of credit reports is beyond the scope of this course, it is important that every real estate investor have at least a basic understanding of how to obtain and read a credit report, as well as be able to do simple credit disputes and repairs.

This credit report knowledge is not only useful when dealing with your own credit, but it is very helpful when dealing with potential buyers and their credit.

#### Your Personal Credit

One of the main purposes of this course is for you to learn how to invest in real estate using no money and no credit. However, as we have already discussed, there are situations when having good credit can make or break a deal. Also, having good credit increases your financing options, which in turn opens more doors to more investment opportunities.

#### Know Your Credit Condition

It is important to learn about your current credit situation so you can establish any limitations you may have on getting new financing. The best way to do this is to sit down with an experienced mortgage broker and go over your credit report. They'll be able to point out problem areas which need to be addressed and they'll tell you what loan programs you should be able to qualify for.

#### If You Have Bad Credit

If you have bad credit it is important to realize that you are not alone. All over the country, millions of hard working and honest people fall into hardship every day. The good news is that no credit is so bad that it can't be repaired over time. In addition, you have legal rights to protect yourself when dealing with your credit and you can repair most errors or discrepancies by yourself.

#### Credit Errors Can Cost You Deals

Even if you know you have good credit, you still need to request a copy of your credit report and make sure there are no discrepancies or mistakes on it.

You don't want to make a loan application and then find out there is an error which will hold up your loan approval. Some errors may take several weeks to resolve. In the mean time, your loan being held up could cost you a deal. If you have not paid particular attention to your credit, then now is the time to do so. In this bonus chapter, you'll learn how to get a copy of your credit report, how to dispute any errors on your credit report, and how to rebuild or expand your current credit.

#### Your Buyer's Credit

The information in the bonus chapter is also very useful when working with buyers who will be getting conventional financing. By knowing how to correct minor credit problems and how to use alternative credit references, you'll be able to sell properties to buyers who might not have been able to qualify for a purchase loan otherwise.

Your knowledge of credit will also help you to better prequalify buyers over the phone and it will help you to more effectively deal with a buyer's loan processor. If you plan to sell properties under a Lease Option, knowing about basic credit repair will be especially important. After all, the lease period is the time which the tenant/buyer should be using to build up their down payment as well as their credit. Investors who are successful at selling under a Lease Option all have a good working knowledge of how to work with a tenant/buyer on any credit problems which are preventing them from getting a loan.

### Understanding Your Credit Report

#### Getting A Copy Of Your Credit Report

The first step to working on your credit is obviously to get a copy of your credit report.

#### Getting A Free Copy Of Your Credit Report

If for any reason you have been denied credit within the last thirty days, you can request a free copy of your credit report. When you receive a credit denial letter, it should list the credit bureau which provided your credit file. Under the Fair Credit Reporting Act, this bureau is required to provide you with a free copy of the credit file they maintain on you, seeing as how you were denied credit based on their file.

If you have not been denied credit in the past thirty days, the credit bureau will supply your credit report to you for a nominal fee, which we'll talk about in just a minute.

#### There Are Three Main Repositories

There are three main repositories. They are Experian, Equifax and TransUnion. Every credit report is created using data from one of these bureaus or a combination of data from two of them, or all three.

#### Ordering Online

All three of these credit bureaus offer online credit reports. This can give you instant access to your credit files.

#### Ordering Over The Phone

You can also order your credit report over the phone.

#### Ordering By Mail



If you don't have internet access, or don't have a credit card for ordering over the phone, you can mail a money order with a written request for a copy of your report. It is best if you call the credit bureau ahead of time to make sure what their current fees are.

- \* First, middle, and last name (including Jr., Sr., III, etc.)
- \* Current address
- \* Previous addresses for the past two years, if any.
- \* Social security number
- \* Date of birth
- \* Current employer
- \* Phone number
- \* Signature
- \* And credit report fee

The following information about yourself should be included as part of your written request. ...  
A sample request letter has been included for you in Exhibit 2.1.

#### Credit Bureau Contact Information

##### Experian

P.O. Box 9595 Allen, TX 75013-0036 888-397-3742 [www.Experian.com](http://www.Experian.com)

##### Equifax

P.O. Box 740241 Atlanta, GA 30374 1-800-685-1111 [www.Equifax.com](http://www.Equifax.com)

TransUnion Consumer Disclosure Center P.O. Box 1000 Chester, PA 19022 800-888-4213 [www.TransUnion.com](http://www.TransUnion.com)

#### Check All Three Repositories

It is very important that you get a copy of your credit report from each of the three credit repositories. Each one of those repositories contain information about your credit and while they do share information, many times there will be a record in one repository that is not in another. It is as if you actually have three different credit reports.

So if you request your credit report from only one of the three repositories, the repositories you did not request a credit report from may contain negative information you need to dispute.

#### 3-in-1 Credit Reports

All three of the main repositories do offer 3-in-1 credit reports. These credit reports contain all the information in your credit file for all three repositories. For the most accurate picture of what your credit files look like, we recommend that you get one of these "combined" credit reports.

#### Contents Of A Credit Report

When it comes to reading a credit report, all three of the main credit bureaus have their own layout and information code system. In the past few years, they have tried to make their credit reports clearer so people can understand them more easily.

All three bureaus do report the same types of information in their reports though. This information includes the following ...

##### Basic Information

Basic information such as your name, address, date of birth, social security number and spouse's name.

##### Credit History

Credit history information listing companies that have loaned you money in the past, along with the account numbers, size of your credit lines, dates the lines were opened, dates you last used the credit lines, repayment terms, amounts you presently owe, status of your payments and number of months your payments are past due.

##### Collection Agencies

They also maintain information on any collection agencies who are assigned to collecting an overdue debt you owe, along with the original creditor's name, the amount it tried to collect, and whether you paid.

#### Additional History Information

Finally, some of the additional information they maintain includes your former addresses, and current (and former) employers.

#### Courthouse Records

In addition, the credit bureaus also maintain information from courthouse records including federal, state or local liens, bankruptcy filings and other judgments.

#### Inquiries

A list of inquiries made by potential credit grantors (like credit card companies), is maintained as well.

## Things That Affect Your Credit Score

One of the most important aspects of your credit report, is your credit score. All three bureaus do create their own credit score for your file, and because each of the repositories use different guidelines for scoring your credit, your credit score will be different at each one.

A credit score is based on a model derived from analyzing the past credit history of thousands of people. Based on the collective credit history of thousands of people with a financial profile similar to yours, the credit score tries to estimate your future behavior in respect to repayment of your loans, making timely payments, etc.

Some of the factors considered when determining your credit score include the following ...

### Payment History

First, is obviously your payment history. If you don't pay your bills on time, you are clearly more of a credit risk and your credit score will be lowered.

### Amounts Owed

How much you owe to your creditors is also a factor. This not only includes how many of your accounts have balances, but how much of each credit line is in use. For instance, if you have a \$5000 available line on your credit card and you owe \$4800, this will pull your credit score down, whereas if you only owed a couple of hundred dollars, you would have a higher credit score.

### Length Of Credit History

The length-of your credit history is very important. The longer your accounts have been open, the more it shows that you can handle long term financial obligations.

### Types Of Credit In Use

The types of credit you have qualified for play a factor in your score as well. For instance, having a department store credit card is not as valuable as a major credit card or home loan.

### Are You Taking On More Credit

If you take on a lot of new accounts within a short period of time, this will also reduce your credit score. New debt is not helpful to your credit report mainly because you haven't had time to create a payment history on the accounts.

Shopping for new credit is just as bad. Many people who are having a tight time with their finances will begin looking for new credit. If you do find the need to apply for credit at several locations, try to do the applications within a fourteen day period. This will help to keep the credit inquiries from affecting your score.

### Unused Credit Affects Your Score

Even unused credit can affect your score in a negative way. If you have numerous open accounts that have zero balances, you still have the ability to access those accounts. While having a couple of unused accounts may not pose a problem, having too much available credit can.

## Disputing Things Off Your Credit

Once you get a copy of your credit report, there are two ways in which to make repairs. The first way is to dispute any incorrect information which your credit report contains. The second way is to payoff any outstanding debts you may owe.

If you have previously made late payments, the only way they can be removed is by either disputing the fact that you were late, or by waiting until the item is so old that it drops off your credit report (this is usually seven years).

In this module, we have included several sample letters for you to use when disputing items on your credit with the credit bureau who is maintaining your credit file.

### Disputing Inaccuracies

If you find that your report has inaccurate information, you can dispute the information and the credit bureau has to investigate it within 30 days. Until the disputed item is proven to be accurate by the creditor, the credit bureau cannot put the disputed information on the credit report unless they include your written statement of dispute.

If you prove that the information is inaccurate, then the information has to be removed from the report permanently within 30 days. A sample letter for disputing inaccurate information is included in Exhibit 2.2.

### Information To Include With Your Dispute

Some of the information you should include in your dispute letter would be the full company name associated with the disputed item, the account number, and reason for your dispute (such as, it is not your account, you have paid the account, etc.)

### Incorrect Information In Your Favor

By the way, if there is any positive miss-information about you or information that is good but not yours personally, don't try to remove or correct it. Even though the information may be incorrect or about someone else, it is on your credit report and helping you.

## Dispute Statements

You can also request that a statement be included in your file. Most credit bureaus allow both the consumer and the creditor to make statements to report what happened, if there is a dispute about something on the report.

## Removing Old Information

Credit reports normally only contain information that is less than seven years old, with bankruptcies remaining for ten years. Anything older than that should have automatically dropped off. If not, you should send the credit bureau a letter similar to the one in Exhibit 2.3.

#### Remove Unauthorized Inquiries

You should also request that any inquiries which you did not authorize be removed as well. Anyone who requested a copy of your credit report should have had your permission ahead of time.

#### Remove Spouse's Information

You can also request that derogatory account information regarding your spouse be removed from your credit report, if you are not liable on the account.

#### Follow Up After 30 Days

As we said earlier, the credit bureau has thirty days to investigate your dispute or request. If after this amount of time you haven't heard back, call the customer service department. There is usually a toll-free number on the credit report you can call for assistance or you can send the credit bureau a letter using the example in Exhibit 2.6. If you call on the phone, remember to keep notes of who you talked to and on what dates.

#### Re-review Your Credit Report

When you do finally get a written response from the credit bureau, by law you should also receive a new copy of your credit report (if there were any changes). You'll want to double check for the changes you had requested, to make sure your credit report is now accurate.

Once any information is changed on the report, the credit bureau cannot change it back unless the creditor provides proof that it was accurate. In this case, you'll get notification from the credit bureau that the item has been put back on your report.

#### Paying Things Off Your Credit

If you owe money to a creditor, and you cannot dispute the item off of your credit report, the only other way to get it off is to pay it off.

There are two ways you can payoff any bad debts you owe ... One way is to payoff the balance with a lump-sum payment (hopefully at a discount). The other way is to payoff the account by making installment payments over a period of time.

#### Dealing With Charge Offs

Some of your past due bills may have become what is referred to as a "charge off". This means that the creditor has either turned your past due account over to a collection service or has otherwise written the account off as a loss. As a result, the account balance shows as an unpaid and overdue balance on your credit. This is very harmful for you if you try to qualify for new credit somewhere else.

#### When To Deal With Charge Off Accounts

The time to deal with creditors on charge off accounts is when you either are able to make one large lump sum payoff or make monthly payments on a regular basis.

#### Paying Off Overdue Accounts In A Lump-Sum

If you decide you want to payoff an account in one lump-sum payment, you should always try to get a discount on the amount you owe.

Furthermore, you're going to request that the creditor remove all negative information on your credit file. Some creditors will not report the payments as on time, but instead will report the charge account as "non-evaluated", rather than "past due" or as a "charge off".

If you want to payoff a debt at a discount, call or write the creditor and let them know that you can't afford to pay the full amount; however, you would at least like to pay off the majority of the account. It is not unusual for creditors to accept 60% or even 50% as payment in full. Simply start by explaining to them your financial condition. Of course, make things look as though they are not getting better, but that you are still credit conscious.

#### A Discounted Payoff May Get You A 1099

It is important to know that if you payoff a debt to a creditor and the creditor forgives a part of the debt equal to \$600 or more, they must send you an IRS form 1099-C at the end of the tax year. This means that when you file your tax return, you must claim the discount as income because of the fact that it was forgiven by the creditor.

The only exceptions to this are ... that you were no longer required to pay the debt because the collection time had expired ... the amount discounted was for late fees, interest or any other charge that was not part of the original principal of the debt. ... or you discharged or eliminated the debt in bankruptcy.

#### Always Get A Signed Release

If you settle on a payoff amount less than the full amount owed, be sure to get the

creditor to sign a release stating that they are accepting partial payment of the debt and that it is accepted as full payment. You'll also want to get them to agree ahead of time to report the account as either "paid as agreed" or "non-evaluated". A release is included at the end of the sample letter in Exhibit 2.12.

You should also put a statement on the front and back of your check stating that "Cashing this check constitutes payment in full of this account".

#### Making Monthly Payments As Payoff

If you can't make a lump-sum payment, your other option is to make monthly installment payments on the debt. Many creditors will settle for a lesser dollar amount when you pay them in a lump sum; however, most creditors will insist on 100% payment of the debt if you pay in monthly payments.

You will want to either call (or write) the creditor and let them know that you had bad financial problems in the past, but you can now afford to make payments.

#### Removing The Past Due Notation

If you get the creditor to agree, have them remove the "past due" notation on the credit file. But realize, as soon as you miss a payment under your new agreement, the creditor will most likely put the past due notation back on your credit file.

If the creditor won't remove the past due notation on your credit file, get back with them in a couple of months after you have made a few payments. State to them that the negative mark on your credit is keeping you from buying a home, getting other credit cards, and so on. Most creditors will remove the derogatory reference if it is keeping you from getting a home loan, so a letter from your mortgage broker would be especially helpful.

#### Re-aging The Account

In return for making monthly payments on the account, you're also going to request that the creditor "re-age" your account. In other words, the current month will show on your credit report as being the first month of the debt being due. It will be as if the account is brand new and as long as you make the payments on time, the account will show as current.

Sometimes the creditor will not re-age the account until you have made at least 2 or 3 consecutive payments on time. This is OK. Just remember to get everything in writing ahead of time.

#### Things To Know When Negotiating

Here are some things you should know when negotiating about payment of your debts.

##### Business Is Business

First, understand that the person who works for a collection agency or creditor is not your friend. He or she may try to build confidence with you regarding your personal problems or show concern for you possibly ruining your credit. Don't believe them. These people have no concern for your well being. Their only concern is to get you to send them money.

##### Negotiate With The Creditor First

Second, always try negotiating with the creditor before negotiating with the collection agency. The creditor will usually be more likely to negotiate seeing as how they are the one who is actually owed the money. On the other hand, if the creditor sold the debt to a collection agency, the collection agency will be the one who you will have to deal with.

##### Negotiate In Writing

When ever you negotiate, always do it in writing. If you do negotiate with someone over the phone, keep good notes regarding the date, who you spoke with, and what was said. Then have them confirm your discussion in writing.

You must have proof of any agreement you and the creditor come to, and you should always get everything in writing before sending any money.

#### How To Send Letters

Here are some important notes you should keep in mind when sending out letters to a creditor or collection service ...

1. First, type your letters or write them very neatly.
2. Keep a copy for yourself.
3. When sending money, use a cashiers check or money order. This way, if you have other debts in collection, the collection agency won't know your checking account number and be able to pass it on to another debt collector.
4. If you're paying off a debt at a discount, always include a statement on the check that "Cashing this check constitutes payment in full of this account".
5. Finally, always send your letter by certified mail and request a return receipt.

#### Negotiation May Take Time

Sometimes the negotiations on an account can take several weeks. So, don't expect to be able to clean up your bad debts within a couple of days. It's better to take your time and make sure that as much of the derogatory information as possible is removed from your file.

#### What If The Creditor Rejects My Offer?

If you are not able to reach an agreement which you can afford, tell the creditor that it

will not work for you and to call you back if they decide to agree with your figures.

If your offer is completely rejected by the person you are dealing with, make sure that you speak with the supervisor. You can also try again a month or so later.

#### Past Bankruptcies

If you have a past bankruptcy, don't worry. You can still get a mortgage loan to buy a property, sometimes as soon as one day after the bankruptcy has been discharge. Of course, these loans come with a substantially higher interest rate and they are even harder to qualify for if the loan is on a non-owner occupied property. In addition, most lenders look for you to have absolutely perfect credit since the bankruptcy and for you to be able to show that you have attempted to reestablish your credit.

There is no way to dispute or otherwise have a bankruptcy removed from your credit report. Bankruptcies stay on your credit report for ten years before they drop off. So, the only way to deal with a past bankruptcy is to work on slowly establishing new credit.

#### Defaulted Student Loans

If you have defaulted on a student loan, the government has what is called a "reasonable and affordable payment program". You and the agency holding your loan decide what is affordable for you based on your income and expenses, and come up with a new monthly payment (even if you have already been sued and there is a judgment against you). As long as you make 6 consecutive monthly payments you will be eligible for a new student loan if you want to return to school. After making 12 consecutive monthly payments the agency holding your loan can remove the default notation from your credit record.

#### Canceling A Student Loan

You may be able to cancel a federal student loan all together if you qualify under one of the following situations ...

You co-signed for a student who dies, you become totally or permanently disabled, you served in the US military, you're a school teacher serving low income students, or a teacher designated in a teacher shortage area, you are a full-time nurse or a medical technician, you're a full-time law enforcement or corrections officer, you're a fulltime worker in a head start program, peace corps or VISTA volunteer, your school falsely certified that you were eligible for a student loan, or the school closed before you completed your program of study.

If you qualify under one of the situations we just stated, you'll want to contact the Department of Education's Debt Collection Service.

#### Building Stronger Credit

Once you have attempted to dispute or payoff any bad items on your credit report, the next step is to work on building your credit report up with positive credit references. This can be done by adding credit references you already have but aren't getting reported, and by establishing new credit references.

#### Strengthening Your Current Credit References

One way to build stronger credit is to try and strengthen the credit references you already have.

#### Increase Your Credit Limits

If you already have a credit card with a low credit limit, ask the creditor to increase it.

Having a major credit card with a substantial credit limit can be very beneficial to your credit score, as long as you keep the account in good standing.

#### No Credit Is Good Credit

If you are starting off with no credit at all, it's important to understand that having no credit is better than having bad credit because your credit report is like a clean slate.

If a potential buyer (or lease option tenant) says they don't have any credit, they are good candidates because of the fact that their credit is not bad. As a real estate investor, all you have to do is work with them to beef-up their credit a little bit. Before you know it, they're sitting there with a loan approval to buy your house.

#### Adding Information To Your Credit Report

The next thing you should do to help build up your or your buyer's credit, is to add credit references to your credit report which are not currently being reported.

#### Spouse's Information

One source for credit references can come from a spouse. If your spouse has good payment histories on some current credit lines, have your name added to the account and then have the account added to your credit report.

If you are already on your spouse's account, but the account does not show on your credit report, you should request that the creditor begin reporting the account in both your names. This is of course assuming that the account is in good standing and has a history of being paid on time.

A sample letter for requesting that a creditor beginning reporting information in both spouse's name is in Exhibit 2.6. You can also have your name added to your parent's credit card account (assuming your parents have good credit). Your parents don't even have to give you a card. Just having your name on the account, is all you need. The credit history of the account will show on your credit report and give you an instant credit history boosting your credit score.

#### Unreported Credit

You should also check your credit report to see if there are any accounts that you are paying on which are not getting reported to the credit bureau. If you find one, contact the creditor and request that they begin reporting your information. If the creditor does not (or will not) report to the credit bureau, an alternative you have is to get the information added as part of a "full factual" credit report.

## "Full Factual" Credit Reports

A full factual credit report is just what its name says, it contains a full set of facts. For an extra fee, a credit bureau will call up a creditor to verify the credit history and then add the information to your credit file. They will also call to verify other information within a short period of time and then update the credit report accordingly. This is a quick way of getting information added or removed from a credit report. This type of service is mainly used by mortgage brokers who need to get a borrower's credit file updated quickly so that the borrower can qualify for a loan. It is also a great way to get alternative credit added to the report when the borrower does not have enough credit references.

## Adding Alternative Credit

Alternative credit references which you could add to your credit report (or your buyer's credit report), include some of the following ...

- \* Electric and water bill payments
- \* Phone bill payments
- \* Unreported car payments
- \* Insurance payments
- \* Various rental payments
- \* Or any other bill you or your buyer pays on a regular basis.

Usually, a mortgage lender will look for a borrower to have at least three credit references. This is something to keep in mind if your credit is weak. Also, if you are pre-qualifying a retail buyer (or lease option buyer) over the telephone who says they have weak credit, you'll want to ask about any alternative credit references they may have.

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## Establishing New Credit

Establishing new credit is a very important step if you have had past credit problems or a bankruptcy.

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If you have no credit at all or really bad credit, the first step will be to get a secured credit card. With this type of credit card, you deposit in an account let's say ... \$500. In exchange, the bank will issue you a credit card with a credit limit of \$500 that is secured by the \$500 you have deposited in the bank.

After making a charge on the credit card, you still have to make a payment to pay the balance off. This type of credit card is not a check card connected to the \$500 deposit you made. The deposit you made ahead of time for \$500 is only security for the bank in case you fail to make the payments as agreed.

After paying on time for six months to a year, you can go back to the bank and request that the card be unsecured, and that you get your \$500 deposit back. You can then make requests every six months or so that your credit limit be increased.

## Good Credit Can Always Look Better

If you already have pretty good credit, qualifying for new unsecured credit shouldn't be much of a problem. Just remember, even if you already have good credit, you should always work to make your credit even stronger and work to get your credit score even higher.

## Avoiding Future Credit Problems

The final step to building stronger credit is to stay out of trouble and try to avoid future credit problems.

## Making A Budget

If you tend to have money problems, start by preparing yourself a budget. Write down all your income sources and then write down every expense that you have each month. (even the little things). Compare them and see if you are overspending, then look for ways you can cut back on your spending.

If you have trouble putting your budget together, you can get help from a nonprofit group such as the Consumer Credit Counseling Service, which can help you for free or at a very discounted cost.

## Paying Your Bills On Time

If you have a bad habit of not paying your bills on time (even when you do have money), set up your monthly payments to be automatically withdrawn from your checking account. This way, you'll never have a late payment, which saves you from paying unnecessary late fees and it helps to keep your credit looking clean.

## Get Overdraft Protection

Having overdraft protection on your checking account is also very important. When applying for a mortgage loan, the lender will usually request your last three month's bank statements. One of the main things they will look for is whether or not you have had any bounced checks. If so, it is an indication that you are having money troubles or just aren't paying enough attention to your finances.

By having overdraft protection, it helps to avoid any future mortgage application problems. It also helps to save you unnecessary bounced check fees.

## Avoid Future Financial Problems

Of course, always try to avoid future financial problems. Here are a few things that will help:

- \* Create a realistic budget and stick to it.

- \* Avoid large house or apartment payments.
- \* Charge for items only when you cannot afford it and it is important that you buy it now.
- \* Don't buy on impulse.
- \* Avoid co-signing or guaranteeing a loan for someone.
- \* And avoid joint accounts with someone who has bad spending habits.

As soon as you see you're going to have a financial problem, you'll need to contact all your creditors and let them know you may have trouble paying your bills at that time. What you want to negotiate with them is two things ... one is the time for you to get back on your feet so you can pay, and two ... you don't want any bad credit information reported to the credit bureau on the account.

#### I Can't Pay My Credit Card Payments!

If you feel you can't pay your credit card or other charge account balance, contact the creditor and let them know of your situation. A lot of times you can have a creditor freeze your credit line and allow you to pay a smaller payment each month. Some creditors will even stop the addition of future interest charges, but few will remove any interest charges that have already accumulated.

In addition, ask the charge company to report your payments to the credit bureau as "on time" while you payoff your balance. As long as you keep to your new payment schedule as agreed, the creditor should not report the debt as past due and they usually don't report the special payment arrangements to the credit bureaus.

#### Excuses Creditors Find Acceptable

When talking to the creditor, start by explaining your problem clearly and let them know the problem will be correcting itself in the future. Here are some excuses as to why you cannot pay your bills that creditors usually find acceptable:

- \* Job layoff or relocation.
- \* Pay cut or cut in hours .
- \* Divorce or separation and your ex-spouse fails to pay their part of the bills even if ordered by court order.
- \* Inadequate medical insurance after a major illness or accident.
- \* Permanent or temporary disability which may include heart attack, stroke, cancer and sometimes a less severe illness.
- \* And finally ... large unexpected tax assessments.

#### Letters To Credit Bureaus

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## Action Guide Workbook

### To Do List

Study the finance strategies covered in this module which require no financing, use existing financing, and that require new financing.

Study how to determine when to use certain finance strategies.

If you are trying to buy your own home, focus on restudying the creative finance strategies used for buying a home.

Find out what local loan programs are available. Call your local Housing Authority and ask if they have a bond program or other type of down payment assistance program.

Have a mortgage broker pull your credit and let you know what kind of loans you can qualify for along with any credit repair needed.

Get a pre-qualification letter for a regular bank loan and for a hard money loan.

Apply for home improvement store cards as a backup source of funds for rehab supplies.

If you have very limited credit, identify alternative credit references which could be included in a full factual credit report.

Request a copy of your credit report. Then dispute any incorrect information. Try to pay any charge offs you may owe if you can afford to.

If you have limited or bad credit, work on strengthening your credit by getting a secured credit card.

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## Quiz

1. What are the three main categories of financing strategies?

1:  
2:  
3:

2. Name the ways to invest in real estate that require "No Financing":

1 :  
2:

3. Name the ways to invest in real estate using "Existing Financing":

1 :  
2:  
3:  
4:

4. Name the ways to invest in real estate that require "New Financing":

1:  
2:

5. What are the five main factors that determine which investment technique to use?

1:  
2:  
3:  
4:  
5:

6. Name four strategies for making money on properties which are 100% financed:

1:  
2:  
3:  
4:

7. When taking over a property "Subject To", you are assuming the loan.

☐ True  
☐ False

8. Land trusts allow you do avoid violating the due on sale clause in a mortgage.

☐ True  
☐ False

9. What is a "short sale"?

10. What is the difference between a private lender and a partner?

11. When paying of a debt to a creditor at a discount, what should you write on the check?

12. If you dispute an item on your credit report, how long does the credit bureau have to complete its investigation of your dispute?

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## Quiz Answer Key

1.  
1: No Financing  
2: Existing Financing  
3: New Financing  
  
2.  
1: Flipping / Quick Turning  
2: Standard Options

3.
    - 1: Subject To
    - 2: Wrap Around Mortgages
    - 3: Agreement For Deed
    - 4: Lease Options
  4.
    - 1: Retailing 2: Rentals
  5.
    - 1: The Seller's Needs
    - 2: Any Existing Financing 3: The Property's Condition 4: Your Financial Abilities 5: Your Investment Goals
  6.
    - 1: Subject To
    - 2: Agreement For Deeds
    - 3: Lease Options
    - 4: Short Sales
  7. False, You are not formally assuming the loan, only making the payments on behalf of the original borrower.
  8. False, Land trusts allow you to disguise who owns the property which hides the fact the property has transferred.
  9. A short sale is where a seller sells their property short of (or for less than) the amount owed on their mortgage. In an effort to keep from having to foreclose on the property, the lender takes a discounted payoff on the amount owed by the seller.
  10. A private lender loans money which is secured by a loan against the property. They do not share in the profits of the deal. A partner puts up the money to buy the property. In exchange, they own an interest in the property and share in the profits of the deal.
  11. Cashing this check constitutes payment in full of this account.
  12. Thirty days.
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## Action Guide Workbook

### To Do List

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