Foreclosure Investing FOR DUMMIES®

by Ralph R. Roberts with Joe Kraynak

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About the Authors

Ralph R. Roberts' success in real estate sales is legendary. He has been profiled by the Associated Press, CNN, and *Time* magazine, and has done hundreds of radio interviews. Ralph is a seasoned professional in all areas of house flipping, including buying homes, rehabbing, and reselling them quickly and at a handsome profit. He has penned several successful titles, including *Flipping Houses For Dummies* (Wiley), *Sell It Yourself: Sell Your Home Faster and for More Money Without Using a Broker* (Adams Media Corporation), *Walk Like a Giant, Sell Like a Madman: America's #1 Salesman Shows You How To Sell Anything* (Collins), *52 Weeks of Sales Success: America's #1 Salesman Shows You How To Close Every Deal!* (Collins), *REAL WEALTH by Investing in REAL ESTATE* (Prentice Hall), and *Protect Yourself Against Real Estate and Mortgage Fraud* (Kaplan).

Foreclosure investing is one of Ralph's many specialties. For over 25 years, he has personally worked in the foreclosure arena, purchasing preforeclosures directly from homeowners, buying foreclosure properties at auction, and often helping homeowners dodge the foreclosure bullet and retain possession of their homes. In *Foreclosure Investing For Dummies,* Ralph reveals his unique win-win approach to investing in foreclosures.

Ralph also serves as Official Spokesman for Guthy-Renker Home, a company dedicated to equipping home buyers, sellers, and real estate professionals with the tools, information, and community setting they need to achieve mutual success. Visit `www.HurryHome.com` and `www.GuthyRenkerHome.com` to experience the exciting innovations that Guthy-Renker Home offers now and is planning for the future.

To find out more about Ralph Roberts, visit `www.AboutRalph.com`.

Joe Kraynak is a freelance author who has written and co-authored dozens of books on topics ranging from slam poetry to computer basics. Joe teamed up with Dr. Candida Fink to write his first book in the *For Dummies* series, *Bipolar Disorder For Dummies,* where he showcased his talent for translating the complexities of a topic into plain-spoken practical advice. He then teamed up with Ralph to write the ultimate guide to flipping houses — *Flipping Houses For Dummies*. In *Foreclosure Investing For Dummies,* Joe and Ralph join forces once again to deliver the definitive guide to profitably investing in foreclosures . . . without selling your soul.

Dedication

From Ralph: To the many investors and Realtors I've worked with, trained, consulted, and coached who have made investing in foreclosures both successful and rewarding.

From Joe: To the investors who use our book not only to build wealth in real estate, but also to assist distressed homeowners and build stronger communities.

Special thanks to Paul Doroh, sheriff-sale and cash buyer for Ralph Roberts Realty, whose priceless insights and real-world experiences transformed our silver into pure platinum. Paul is a mighty fine writer, even by Joe's standards, and without his late inning relief, this book would not have been possible.

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Although we wrote the book, dozens of other talented individuals contributed to its conception, development, and perfection. Special thanks go to acquisitions editor Lindsay Lefevere, who chose us to author this book and guided us through the tough part of getting started. Jennifer Connolly, our project editor, deserves a loud cheer for acting as a very patient collaborator and gifted editor — shuffling chapters back and forth, shepherding the text and photos through production, making sure any technical issues were properly resolved, and serving as unofficial quality control manager. We also tip our hats to the production crew for doing such an outstanding job of transforming a loose collection of text and illustrations into such an attractive bound book.

Throughout the writing of this book, we relied heavily on a knowledgeable and dedicated support staff, who provided expert advice, tips, and research, so we could deliver the most comprehensive and useful information. Lois Maljak proved invaluable not only as a resource person but also as the communications hub for the flurry of files and e-mail messages flying back and forth on a daily basis. Thanks also to Ralph's number-one virtual assistant Kandra Hamric, who helped us tie up all the loose ends and put the appendix together.

We owe special thanks to our technical editor, accomplished real estate pro Blanche Evans, for ferreting out technical errors in the manuscript, helping guide its content, and offering her own tips and tricks.

Publisher's Acknowledgments

We're proud of this book; please send us your comments through our Dummies online registration form located at www.dummies.com/register/.

Some of the people who helped bring this book to market include the following:

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Contents at a Glance

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Introduction

To the average homeowner, people who buy and sell foreclosures are greedy opportunists at best and scum of the earth at their very worst. Foreclosure investors prey on unfortunate homeowners — families who, through no fault of their own, can't afford to make their next house payment. Investors swoop in, scoop up properties for pennies on the dollar, and then turn around and sell those properties for huge profits, laughing all the way to the bank.

That's the stereotype of foreclosure investors, and many "investors" certainly fit that stereotype, but real investors, the ones who operate with integrity, compassion, and a sense of fairness, the ones who are most successful as long-term investors, don't play that game. They know that homeowners are not facing foreclosure because they enjoy being hassled by bill collectors and threatened with eviction. Distressed homeowners have reached this point due to some financial setback or oversight, a job loss or layoff, health issues or the death of a family member, human foibles, or a host of other causes that happen to be a natural part of life. Most of these homeowners are so humiliated that they won't even ask loved ones for help.

Sure, foreclosure investors want to make a profit. Unless they were selfless philanthropists, they wouldn't even consider investing their time and money without having some profit motive to do so. Investors with integrity, however, strive toward developing solutions that are fair and less painful for all parties involved. Some investors are actually in the game to improve their communities — some are churches reinvesting in their neighborhood. Without these investors, homeowners would have fewer options, actually only two options — come up with the cash or be forcefully evicted. Many would be forced out of their homes with nothing to show for it. Lenders would have to play hardball. Governments would face the increased burden of picking up the pieces.

I don't want you to become a stereotypical foreclosure investor. I want you to join the ranks of successful, fair-minded investors who present homeowners with a menu of options from which to choose and offer to purchase their home at a reasonable price that earns you a reasonable profit. I want you to assist distressed homeowners in assessing their options, choosing the option that's in their best interest, and then taking the necessary steps to put an unfortunate incident behind them and move on with their lives.

Following the advice I offer in this book won't guarantee a profit on every investment opportunity that comes your way. You'll encounter many homeowners who shun your advice. You'll miss a few golden opportunities to score some quick cash. You may even lose opportunities to less ethical investors who offer the homeowners empty promises. You'll soon discover, however, that by treating distressed homeowners with compassion and a sense of fairness, you have more opportunities than you have time and resources to pursue. Through your hard work and integrity, you will achieve a higher level of personal and financial success than the less ethical investors in your neighborhood who are simply conforming to the age-old stereotype.

About This Book

This book is no quick-cash, no-risk, no-work guide to building wealth through foreclosure investing. People who want that sort of thing can stay up late at night and listen to the real estate investment gurus peddle their products, or they can attend any of the readily available "free" foreclosure investment seminars that make their rounds.

This book guides you in the methods of making money the old-fashioned way — earning it fairly. I've been investing in foreclosures and assisting distressed homeowners for more than 30 years. I have achieved great success and have experienced my fair share of failures. I've had homeowners provide glowing testimonials of how much I've helped them, I've been accused of trying to steal homes from "little old ladies," and I've assisted homeowners when con artists have actually tried to steal their homes. Sad to say, I have even lost property in foreclosure myself.

In *Foreclosure Investing For Dummies,* I show you how to invest in foreclosures the right way. I steer you clear of the many pitfalls inherent in foreclosure investing. I show you how to properly and thoroughly research properties, so you know what you're getting into before you buy or bid on a property. I step you through the process of finding the best opportunities with the maximum potential profit and lowest risk. I lead you through the process of buying foreclosures prior to auction, bidding for them at auction, and purchasing them after the auction from the lenders that have foreclosed on them. I present various ways to cash out and realize your profit after the sale. And I show you how to do it without misleading and cheating distressed homeowners.

Conventions Used in This Book

Compared to other foreclosure investing programs and books, *Foreclosure Investing For Dummies* is anything but conventional, but I do use some conventions to call your attention to certain items. For example:

- *Italics* highlight new, somewhat technical terms, such as *redemption period,* and emphasize words when I'm driving home a point.
- **Boldface** text indicates key words in bulleted and numbered lists.
- `Monofont` highlights Web addresses.

In addition, even though you see two author names on the cover of this book — Ralph and Joe — you see "I" throughout the book when I, Ralph, am describing my personal experiences with foreclosure investing and offering my expert advice. Joe's the wordsmith — the guy responsible for keeping you engaged and entertained and making sure I've explained everything as clearly and thoroughly as possible.

What You're Not to Read

Although I encourage you to read this book from cover to cover to maximize the return on your investment, *Foreclosure Investing For Dummies* facilitates a skip and dip approach. It presents the information in easily digestible chunks, so you can skip to the chapter or section that grabs your attention or meets your current needs, master it, and then skip to another section or simply set the book aside for later reference.

I do, however, consider Chapter 8 required reading. All too often, investors fail to properly research a property, and they really get burned. Chapter 8 shows you how to collect key information about a property, so you know what you're buying before you invest tens or hundreds of thousands of dollars in it.

If you read my book *Flipping Houses For Dummies* (Wiley), you can safely skip Chapter 17 because *Flipping Houses For Dummies* covers the process of repairing, renovating, and preparing a home for sale in much greater detail and even includes plenty of before and after photos.

You can also safely skip anything you see in a gray shaded box. I stuck it in a box for the same reason that most people stick stuff in boxes — to get it out of the way, so you wouldn't trip over it. However, you may find the stories and brief asides uproariously funny and perhaps even mildly informative (or vice versa).

Foolish Assumptions

In some books that cover advanced topics, authors must assume that their readers already understand some basic topics or have acquired beginning-level skills. For example, if this were a book about molecular biology, you'd have to know what a molecule was.

The biggest foolish assumption I make in this book is that you own the home you live in. You've been involved in at least one closing and signed the documents that the closing agent passed around. When you own a home, you instantly become a real estate investor. You begin to grasp the value of real estate as an investment. You gain first-hand knowledge of the benefits of owning a home, understand the challenges of maintaining it, and take on the responsibility of making mortgage payments. You can empathize with homeowners who are about to lose their homes in foreclosure.

If you're not a homeowner, sell this book and put the proceeds toward a down payment on a house. If you live in the Detroit metropolitan area, gimme a call, and I'll find the perfect house for you and your family. I'll even give you credit on the purchase of the book, or stop by the office, and I will personally sign your copy. Once you've purchased a house and have lived in it for a few months, pick up the book. I'll be waiting for you.

Other foolish assumptions I make include but are not limited to the following:

- **You're committed to success.** Investing in foreclosures is hard work and requires *sticktoitism* (pronounced stik-to-it-izm) — a word I've been using since the 1970s to describe the determination and dogged perseverance required to build wealth in real estate. I could use "stick-to-itiveness," which happens to appear in the dictionary, but I like my word better.
- **You can talk to people.** You don't need to be a social butterfly (although that helps), but you do need to be able to network, ask questions, and haggle with people. If you don't have some basic people skills, you should team up with someone who does. Effective word-of-mouth networking leads to the best opportunities, and in almost every situation you'll need to talk with homeowners, county clerks, sheriffs, lenders, and a host of others involved in the foreclosure process.
- **You're dedicated to developing mutually beneficial solutions.** I hate to see "investors" ripping off homeowners, and I would really hate to see anyone use the information in this book to take advantage of distressed homeowners. You can make plenty of money investing in foreclosures by acting with integrity and presenting reasonable solutions that meet the needs of all parties involved.
- **You can treat foreclosure investing as business.** Understand that you are not the cause of the homeowners' distress. More than likely, you cant' solve their problems. Very likely, many others have tried to help the homeowners solve the root cause of the problem (and failed) before you came along. What you can offer is truth and useful information. You must be empathetic without jumping in to save a drowning family that may drag you under both financially and emotionally.

A problem is something that money can't fix, such as an untreatable illness or a death in the family. Most families, if they choose to, can move on after experiencing a financial calamity. Foreclosure is not the end of the world, although, at the time, they may perceive it to be.

How This Book Is Organized

I wrote this book so you could approach it in either of two ways. You can pick up the book and flip to any chapter for a quick, stand-alone mini-course on a specific foreclosure-investing topic, or you can read the book from cover to cover. To help you navigate, I took the 22 chapters that make up the book and divvied them up into six parts plus an appendix. Here, I provide a quick overview of what I cover in each part and in the appendix.

Part I: Prepping Yourself for Foreclosure Success

Before you can successfully invest in foreclosures, you have to wrap your brain around the foreclosure process, be able to identify where the opportunities lie, and understand the risks. In this part, I bring you up to speed in a hurry on the foreclosure process, assist you in picking your point of entry, and offer tips on how to avoid the most common pitfalls.

Part II: Laying the Groundwork for Maximized Profit and Minimized Risk

Some people invest more time and energy planning for a two-week vacation than they spend planning for a foreclosure investment. By skipping the preparation steps, they almost guarantee failure. In this part, I show you how to obtain the information, tools, support, and resources you need to improve your chances of success. You find out how to assemble a team of talented professionals and other key players qualified to deal with issues that you may not be prepared to handle. You discover sources of investment capital you may not have considered. And you pick up a few networking strategies that can lead you to the best deals before other investors pick up the scent.

Part III: Creating Win-Win Situations in Pre-Foreclosure (Prior to Auction)

Some of the best foreclosure investment opportunities are available in pre-foreclosure — purchasing a home directly from the homeowners prior to auction. Competition from other investors is generally less fierce at this point, and the homeowners have more options. In this part, I show you how to locate properties prior to foreclosure, gather information about those properties and their owners, and assist homeowners through the foreclosure process while acquiring properties below market value.

Part IV: Finding and Buying Foreclosure and Bankruptcy Properties

Many investors prefer not to deal directly with distressed homeowners in pre-foreclosure. They'd rather purchase the property at auction and then work on their end game. In this part, I show you how to find and buy properties at auction, from banks and other lending institutions that repossess properties, from trustees during bankruptcy, and from various government agencies and government-sponsored programs.

Part V: Cashing Out Your Profit . . . after the Sale

You make your money when you buy a property — by purchasing it below market value — but you realize that profit when you sell, lease, or refinance the property. In this part, I reveal various ways to cash out on your investment. I offer strategies for encouraging the previous homeowners to vacate the premises voluntarily, and I show you how to initiate eviction, if the homeowners refuse to leave. You discover how to maximize your profit by repairing, renovating, and either selling or leasing the property, and you pick up tips on various other strategies for profiting from your investment.

Part VI: The Part of Tens

The Part of Tens is the highlight of every *For Dummies* title, offering quick strategies, tips, and insights on whatever subject the book covers. The chapters in this Part of Tens show you how to avoid the ten most common beginning blunders and offer ten ways to assist homeowners in navigating the foreclosure process in a way that convinces the homeowners to work with you rather than with some other investor.

Icons Used in This Book

Throughout this book, I've sprinkled icons in the margins to cue you in on different types of information that call out for your attention. Here are the icons you'll see and a brief description of each.

I want you to remember everything you read in this book, but if you can't quite do that, then remember the important points I flag with this icon.

Tips provide insider insight from behind the scenes. When you're looking for a better, faster, cheaper way to do something, check out these tips.

"Whoa!" This icon appears when you need to be extra vigilant or seek professional help before moving forward.

Where to Go from Here

Foreclosure Investing For Dummies is constructed in a way that's similar to the foreclosure process itself. It presents you with opportunities and with information to capitalize on those opportunities in three key entry points in the foreclosure process: pre-foreclosure, foreclosure, and post-foreclosure.

For a quick course on foreclosure investing, check out Chapter 1, which provides an overview of the foreclosure process along with some tidbits on how to profit from the various stages of the process. Skip to Chapter 3, where I guide you in selecting your preferred entry point. The chapters in Part II are indispensable in preparing you for a successful investment venture. If you choose to invest in pre-foreclosures, skip to Part III, were you discover how to research properties and deal directly with homeowners. (Part III also contains a chapter — Chapter 8 — that's essential for all foreclosure investors — properly researching a property.) If you're interested in purchasing properties at auction or after they've been repossessed, Part IV provides all the information you need to know. And when you're ready to cash out on your investment, skip to Part IV.

In a few chapters I include fill-in-the-blank forms and worksheets you can scribble on. Although you can fill out these forms and worksheets in the book, you may want to make copies to write on. These forms and worksheets are indispensable in gathering research data, evaluating properties, and presenting options to homeowners facing foreclosure.

Part I

Prepping Yourself for Foreclosure Success

The 5th Wave By Rich Tennant

"Hi, Honey! I just got a great lead on a foreclosed property. By the way, how do you feel about ghosts, ancient burial grounds and curses?"

In this part . . .

Achieving financial success by investing in foreclosures requires a good deal of preparation. You need to understand the foreclosure process in your area, pick a stage in the foreclosure process as your area of expertise, and become well aware of the pitfalls to avoid. Only with the proper preparation can you minimize your risk and maximize your potential profit.

The chapters in this part bring you up to speed on the foreclosure process, assist you in picking a point of entry you want to focus on, and steer you clear of some of the major and common pitfalls that trap novice foreclosure investors.

Chapter 1

Wrapping Your Brain around Foreclosure Investing

In This Chapter

- Taking a bird's-eye view of the foreclosure process
- Building a team of advisors, investors, and assistants
- Gathering critical data about properties and their owners
- Buying and taking possession of a foreclosure property
- Realizing your profit at the end

Whenever you're developing a new skill, having an overview of the process provides you with a context for understanding. In the case of investing in foreclosures, a general knowledge of the foreclosure process and the rules and regulations that govern it can reveal opportunities for purchasing properties below market value.

Understanding the necessity of having a strong investment team in place enables you to begin thinking about the people who would be best qualified to assist you. And realizing the benefits of thorough research can prevent you from buying a property that's destined to send you to the poorhouse.

In this chapter, I provide an overview of the foreclosure process, stress the necessity of building a competent investment team, introduce you to essential property research techniques and resources, briefly explain the process of buying and taking possession of properties, and touch on various options you have to cash out your profit once you own the property. In a nutshell, I give you the basic structure for investing in foreclosed properties, and as soon as you begin buying foreclosure properties, you can start plugging in the details — attention to detail is the key to success.

Investigating the Foreclosure Process from Start to Finish

A common misconception of foreclosure is that after the homeowners miss a payment or two, the lender immediately takes possession of the property and then turns around and auctions it off at a foreclosure sale. Actually, the process is more drawn out than that, following this typical scenario:

- Homeowners stop making mortgage payments.
- After about 15 to 30 days, lender sends a payment reminder.
- If the homeowners still don't respond, the lender continues to send notices and call the homeowners.
- If the homeowners still don't contact the lender, the lender turns the matter over to its collection and harassment department, who continues to pester the homeowners with letters and phone calls.
- After about three missed monthly payments, the lender transfers the matter over to outside counsel, which is normally handled regionally. The attorney sends an official notice, warning that foreclosure proceedings are about to begin.
- Homeowners don't reply or present a solution that the lender deems unsatisfactory. At this point, the homeowners can usually stop the foreclosure by negotiating a suitable solution with the lender.
- The attorney begins the foreclosure process by posting a foreclosure notice in the county's legal newspaper or in the local newspaper. The homeowners can still *reinstate* the mortgage at this point by catching up on the payments and paying any additional late fees and penalties, which occurs quite often. See Chapter 9 for details on how to track foreclosure notices. (The county legal newspaper serves the public and provides the legal community with an automated system, but these are private, for-profit publications, not freebies that the county publishes.)
- The property arrives at the civil division of the sheriff's office, which is assigned the task of handling the sale. The trustee or attorney handling the foreclosure sets the opening bid and typically advertises it in the foreclosure notice. The opening bid is the balance of the mortgage plus penalties, unpaid interest, attorney fees, and other costs that the lender has incurred during the process.
- The sheriff or his representative may visit the house prior to the sale to post a foreclosure notice and inspect the property, because sometimes redemption rights change if the homeowners abandon the property. (Some states have a *redemption period,* after the sale, during which time the homeowners can buy back the property by paying the full amount of the loan along with taxes, interest, and penalties. This period can last up to a year.)

- The day before the auction, the lender may adjust the price up or down, but may not artificially inflate it. Frequently, lenders reduce the opening bid to make the property more appealing to investors and rid themselves of it.
- Property goes on the auction block for sale to the highest bidder or is turned over to a trustee to liquidate the property and pay the lender.
- An investor purchases the property at auction or from the trustee, or the lender buys the property. If nobody bids higher than the opening bid, which the foreclosing lender submits, control is handed over to the lender, who can then take possession of the property following any redemption period as explained next.
- In some states, the high bidder (or lender, if nobody bids more than the opening bid) takes immediate possession of the property. In states with a redemption period, the new "owner" must wait until the redemption period expires and a final court hearing with the homeowners before they can do anything with the property. If the lender takes possession of the property, the lender transfers the property to its REO (Real Estate Owned) department, which prepares it for sale.
- Previous owners move out or are evicted.

The foreclosure process is a lose-lose situation for both the homeowners and the lender. The homeowners lose the property, and the lender takes a loss on the loan and often pays additional costs to resell the property to recoup a portion of its loss.

REMEMBER

If you or a loved one is ever facing a foreclosure, contact the lender immediately to explore your options. Seek help sooner rather than later. Shame, anger, and denial may discourage you from seeking assistance, but the longer you wait, the fewer your options. Educate yourself and communicate with your lender. Homeowners who panic become very vulnerable to foreclosure rescue schemes. Do your research, know your options, and don't deal with someone who's claiming to be your friend. A good place to seek help is Freddie Mac's Don't Borrow Trouble Web site at www.dontborrowtrouble.com.

For more in-depth coverage of the foreclosure process, including variations in different areas of the country, skip to Chapter 2.

Picking Your Point of Entry

As a real estate investor, you can step in at any stage of the foreclosure process to acquire properties and enact other profitable transactions:

- **Pre-sale:** Before the property is auctioned or transferred to the trustee.
- **Sale (or auction):** When the sheriff or the court auctions the property or after control of the property is placed in the hands of the trustee.
- **Post-sale:** After the lender repossesses the property, you can purchase the property from the lender or from its REO broker.

In the following sections, I describe these three entry points. For more advice on how to select an entry point that's right for you, refer to Chapter 3.

TIP

Begin tracking properties early in the process, even if you choose to buy properties later in the process. By tracking properties early, you pick up on the history of what's going on and develop a clearer idea of how much to pay for the property.

Scooping other investors during the pre-auction stage

As soon as homeowners realize that they can't make their payments, you can mediate between the homeowners and their lenders to work out a mutually acceptable solution. In a few cases, you can help the homeowners keep the property; for example, by negotiating a *forbearance* with the lender that provides the homeowners extra time to catch up on their payments.

Did I just say "help the homeowners keep the property?" Yes, your long-term best interest is best served by doing what's best for the homeowners. Sometimes that means you receive no profit from your efforts. In a huge percentage of cases, however, the homeowners' best option is to sell the property and find more affordable housing arrangements. By being sincerely concerned with their best interests, you place yourself in a position to acquire the property if the homeowners can't or won't take the action necessary to keep it.

TIP

Your goal during the pre-foreclosure stage is to present the distressed homeowners with all of options and enable them to make well-informed decisions. See Chapter 9 for a complete list of options.

Stepping into the foreclosure process during the pre-auction stage provides you with some of the best opportunities to assist the homeowners and purchase a property at an attractive price. In Part III, I show you exactly how to research and buy homes before homeowners lose them in foreclosure.

Bidding on properties at foreclosure auctions

Some investors prefer to step into the process at the auction stage, because they're uncomfortable dealing with distressed homeowners who are often in a state of denial and unwilling to sit down with an investor to discuss their options. At the auction stage, you buy the property in a less emotional atmosphere. In most cases, however, you still have to deal with the homeowners when the time comes to take possession of the property.

Now, don't run out and start scooping up properties at foreclosure auctions just yet. Uninformed investors often get burned by diving before they learn to dog paddle. Foreclosure auctions are packed with peril, often trapping novice investors into making costly mistakes, such as these:

- **Buying a property without researching the title.** A title history reveals who really owns the property and the amount currently owed on the property, and the priority of the mortgages — tax lien (top priority), first mortgage (next in line), second mortgage, and so on. Do your research, as explained in "Doing a Little Detective Work," later in this chapter and in Chapter 8.
- **Buying a junior lien thinking it's a senior lien.** When you buy "properties" at a foreclosure sale, you're really buying mortgages. The first mortgage on a property is called the *senior lien,* which gives the buyer the most control over the property. Additional claims against the property are called *junior liens,* which often get wiped out during foreclosure. Buy a junior lien by mistake, and you may have just bought yourself a worthless piece of paper. Only a thorough research of the title, as explained in Chapter 8, can steer you clear of making this common and potentially very costly mistake.
- **Buying a property without inspecting it.** A house may look valuable on paper, but until you see it with your own eyes, you don't know for sure. The house may have significant fire damage, toxic materials, foundation problems, or a host of other defects. Check out Chapter 8 for details.
- **Paying more for a property than what it's worth.** In the heat of an auction, your enthusiasm to outbid fellow bidders often leads novice investors into paying more for a property than what it's worth. This almost guarantees that you'll end up taking a loss on the property.
- **Failing to account for the redemption period.** Most states have a mandatory redemption period, during which time the homeowners retain possession of the property and can redeem the title by paying off the mortgage in full along with any penalties and back taxes. You need to have enough cash reserves on hand to pay the property taxes on the property and to insure the property during this time. If you don't pay the property taxes, another investor may be able to purchase a tax lien or deed at a tax sale and take control of the property — tax liens have priority. You also need to insure the property, because you're not covered by the homeowner's insurance policy (if they have one).

Don't forget the insurance

As soon as you buy a foreclosure, even if you can't take possession of it right away, call your insurance agent and buy a homeowner's insurance policy for the property.

I purchased a house for $75,000 that was worth $150,000. By the time I took possession of the property, the previous owner had taken the carpeting, the entire kitchen including the kitchen sink, the bathroom fixtures, the furnace the central air conditioning unit, the doors, and anything else they could carry out hoping to cause harm to the next owner. I turned it into my insurance carrier, received $25,000, and sold the house for $100,000 to another investor. After expenses and holding costs, I walked away with about $35,000.

The investor who bought the property decided to rent it out instead of selling right away. He refinanced to pull about $50,000 equity out of the property, used the equity to cover repair and renovation costs, and still had a little money left over. He then rented out the property to cover his mortgage payments.

Never bid on a property at auction until you've done your homework. Reading this book from cover to cover is a start. Brush up on the foreclosure rules and regulations in your area, and always research a property thoroughly before bidding — research the title and inspect the house as closely as possible with your own two eyes, as shown in Chapter 8.

Buying properties after the sale

Working with homeowners prior to auction and waging bidding battles against other investors during an auction may not appeal to you, but you can still profit from investing in foreclosures after the foreclosure sale.

If nobody at the auction offers the minimum acceptable bid, the lender buys back the mortgage. If the state has a mandatory redemption period, the lender waits until the period expires and then passes the property to its *REO* (Real Estate Owned) department (sometimes referred to as the *OREO* or Other Real Estate Owned department, not to be confused with the cookie), which prepares the property for resale and typically hires a mortgage broker to place it back on the market. By dealing with a lender's REO department or its mortgage broker, you may be able to purchase the property at a price that's discounted far enough below market value to turn a profit of 20 percent or more.

The chapters in Part IV show you how to find and buy REO properties and other properties that government institutions and law enforcement agencies take possession of and then often sell at deep discounts:

- Properties seized due to nonpayment of taxes
- Properties seized by customs and law enforcement agencies because the properties were paid for with profits from illicit activities
- HUD (Housing and Urban Development) and VA (Veterans Administration) houses that were repossessed when homeowners defaulted on HUD or VA loans
- Fannie Mae and Freddie Mac properties that were repossessed and then turned over to these government-sponsored loan programs
- Bankruptcy properties that are being liquidated to pay off loans
- Properties that the Department of Transportation purchased for road improvements and then must dispose of after completing the improvements

When buying a property from the government or a bank, don't assume that you're getting a good deal. Homes are typically sold in their "as is" condition. You must still research the title carefully and inspect the property with your own two eyes. If you see ads or late-night infomercials selling lists of bank-owned properties, don't fall for the hype — these lists are usually outdated long before they arrive in your mailbox.

Assembling a Team of Experts and Advisors

Flying solo on foreclosures may seem like a good idea. After all, if you get other people involved, they may become rivals and pick up on your carefully guarded secrets. Flying solo, however, is a good way to go bust or at least limit your potential profit. Developing synergistic relationships with top performing specialists has been a key to my success and the success of almost all of the top real estate investors around the world.

In addition to providing expert guidance and advice for seizing opportunities and avoiding common pitfalls, experts deliver leads to potentially profitable properties, affordable financing, and quality contractors. They can assist you in managing your finances and in renovating and selling your property for top dollar after you purchase it. And, by delegating some of the workload to others who are better equipped to handle it, you free up time and resources for finding the most profitable opportunities.

Stand by your man — or woman

Tell your spouse or significant other about your plans to invest in foreclosure properties and ask for help. If your spouse is a couch potato and would prefer to remain anchored to a lounge chair over helping you work nights and weekends, then you're likely to find yourself swimming upstream — right into a concrete dam.

Your better half needs to know that you're planning on earning tens of thousands of dollars per deal, and since he is surely going to want to spend some of that money with you, he'd better dig his potato out of that chair and help.

I strongly recommend against any attempts to invest in foreclosures without the full consent and eager assistance of your spouse. I would hate to hear that after reading this book, you and your better half stopped calling each other "honey" and "sweetie pie" and started calling each other "plaintiff" and "defendant."

In Chapter 4, I show you how to assemble a solid foreclosure investment team consisting of the following members:

- Real estate agent
- Real estate attorney
- Mortgage broker
- Accountant
- Title company
- Home inspector
- Contractors

In Chapter 5, I lead you to sources of financial capital to fuel your investments, and in Chapter 6, I lead you through the process of developing a strong support network that virtually ensures that you'll never run out of leads to profitable foreclosure properties.

REMEMBER

With a solid team in place, you take on the role of manager and major decision maker and can create an efficient system that minimizes risk while maximizing profit.

Getting Your Financial Ducks in a Row

In real estate, cash is king. In foreclosure investing, cash is the grand, high-exalted mystic ruler. Investment capital enables you to step in at any stage of the foreclosure process and buy out anyone who has a claim on or an interest in the property.

When I say "cash," I'm not just talking about the money you have stuffed in your mattress. I'm talking about borrowing certified funds from a bank or other lending institution. See Chapter 5 for details.

Cash gives you the upper hand with the four Cs:

- **Credibility:** With cash, you have instant credibility that you can deliver on your promises without hesitation. In most cases, homeowners need cash to escape their current financial crisis. Lenders need cash to cut their losses. With cash on hand, you can give homeowners and lenders enough to achieve their goals, while you take possession of a profitable property.
- **Confidence:** Cash provides you with the confidence you need to pitch offers to both homeowners and lien holders, knowing that you can deliver in a timely manner.
- **Creativity:** Putting together a foreclosure deal that satisfies all parties often requires a great deal of creativity. With sufficient capital, you liberate your imagination from financial limitations.
- **Competitiveness:** Multiple real estate investors often compete for the same property. Cash gives you a competitive edge, because it enables you to execute a deal much more quickly. Both homeowners and lenders are eager to put the current crisis behind them. An ability to act quickly often separates the successful investor from the wannabes.

The question of "Where am I going to get the money?" often derails the novice investor before the train leaves the station, but many of the most successful investors started out with only a few bucks in their pockets, including yours truly.

Don't let a lack of investment capital discourage you. In Chapter 5, I show you how to estimate just how much money you need to get started, and then I steer you toward sources of capital to fuel your foreclosure investments. At first, the cost of investment capital may chip away at your profits, but as you develop a stronger financial position, the cost of money gradually decreases.

Doing a Little Detective Work

When you decide to invest in foreclosure properties, you take on the role of private detective. To protect yourself from the many inherent risks of foreclosure investing, dig up the essential facts and figures, so you know what you're buying, what it's worth, and your options for purchasing the property for less to maximize your profit.

Thorough research requires that you dig up the following essential information:

- Names of the homeowners
- Amount owed on the property
- Lien-holder names and contact information
- Physical condition of the property
- Homeowners' current situation and motivations
- Market value of the property

The following sections introduce you to the types of research to perform as part of your due diligence, but proper research requires much more than I can cover in this short chapter. For additional details, see Chapters 8 and 9.

Finding foreclosures and seized properties

The first step in foreclosure investing is often the most difficult for first-time investors — finding potentially profitable properties. Plenty of foreclosures and seized properties are available, but where do you look for them? The answer to that question varies depending on where in the foreclosure process you choose to focus on, but here's a list of where you can expect to obtain the most valuable leads:

- The neighborhood grapevine, including neighbors, churches, local cafes, clubs, and even people contacting you directly for assistance when they know that you buy distressed properties
- Foreclosure notices in local papers or legal publications
- Bankruptcy notices in local papers or legal publications
- Divorce filings and decrees in publicly accessible court documents
- Web sites that list foreclosure and government-seized properties
- Real estate agents
- Attorneys, particularly bankruptcy, divorce, and probate attorneys
- Lenders

Online foreclosure information services range from excellent to total rip-offs. Some services deliver timely information, while others deliver out-of-date information that's totally useless. In the beginning, you should do your own footwork.

Word-of-mouth leads are often the best leads. Make sure everyone you know and meet knows that you purchase distressed properties and work with people who are facing foreclosure. Some investors have so many distressed homeowners contacting them for assistance in foreclosure that they don't even have to look for properties. See Chapter 6 for networking tips.

Investigating the property's title and other documentation

Before you commit to purchasing a property, you have to know who really owns it, how much the current owners owe on it, to whom they owe the money, how much they owe (if anything) in back taxes, and whether the property has any *encumbrances* (liens, judgments, or zoning restrictions) on it. In short, you need to know what you're getting yourself into before you get yourself into it.

Fortunately, most of the critical documentation about a property is accessible to the general public and the title company you use:

- **Title:** The title shows the names of the property owners and lien holders and any legal judgments on the property. I once purchased a property from a mother and daughter, only to discover later that the daughter I bought the property from wasn't the daughter who owned it. The right daughter eventually took possession of the property, and I was left with some nasty, time-consuming legal battles. By checking the title, you can avoid similar mistakes.
- **Title history:** A title company can provide you with a title history that shows the change of ownership over the years. In some cases, this history reveals gaps in the transfer of the property from one homeowner to the next. A gap in the history may be a warning that someone else can lay claim to the property later and take you to court.
- **Property history:** Your town or city keeps a history of every property, which includes all building permits issued on the property. If the property has an additional structure that was built without a permit, it may not have been built to code. Any information you can gather about the history of the property can assist you later in evaluating its market value.

Never purchase a property without fully researching its title and any other public documents recorded on that property. In Chapter 8, I guide you through the process of researching a property and assembling a detailed dossier, which is essential for making sound investment decisions.

Inspecting the property with your own eyes

Tattoo the following message on your forehead: *my eyes or no buys.* You can look at the title work and other property documents until your eyes cross, but you don't know the condition of the property unless you see it for yourself:

- **Visit the property and the neighborhood it's in.** Never try to assess the value of a property in a vacuum. The condition of the neighborhood affects the sale price.
- **Walk around the property and inspect it from all four sides.** The front of the house can look like the Taj Mahal, while the back or sides look more like a bombed out bunker.
- **If possible, get inside to take a look around.** You don't want to get picked up for voyeurism or run off by an angry homeowner, but if the homeowner invites you in, accept the invitation. See Chapter 8 for additional suggestions on doing drive-by and walk-around inspections.

TIP

If the house is currently listed with a broker, make an appointment to view the house. This is an excellent way to get the inside scoop without being accused of being a peeping Tom! You don't have to tell the broker what you know about the property or why you're interested in it.

See Chapter 8 for more tips on inspecting the property with your own two eyes.

TIP

This cursory inspection offers you only a glimpse of the property, and in foreclosure investing, sometimes that's all you get, especially if you're purchasing the property at an auction. When buying a property prior to auction directly from the homeowners, make your offer conditional upon a satisfactory inspection, and then have the property professionally inspected before closing to uncover any costly defects and provide a ballpark estimate of the cost of repairs and renovations needed to bring the property up to market value. If the property requires repairs, try to negotiate a price reduction, instead of canceling the deal; for example, if the repair costs $2,500 try to get a reduction of $3,500.

Guesstimating a property's true value

An essential component of successful real estate investing is developing an exit strategy or end game. Before you agree to pay a certain price for a property, you must have a fairly accurate estimate of what you can sell it for. Otherwise, you risk overpaying and losing money on your investment.

Estimating the market value of a house is easiest with the assistance of a real estate agent who's knowledgeable about property values in the area. A qualified agent can pull up MLS (Multiple Listing Service) sheets on comparable homes that have recently sold in the same neighborhood and quickly provide you with a good idea of how much you can sell the property for, assuming it's in marketable condition and the market remains relatively stable.

Don't let your agent or the word on the street pump up your expectations or estimates. Tell your agent that you want an estimated sales price based on what the agent is sure she can get, not what she hopes she can get. Provide your agent with as many details as possible about the property, so she can look up similar properties that are truly comparable to the one you're thinking of buying.

Never enter into a real estate deal unless you have at least two exits — a plan A, typically for selling the property at a profit, and a plan B just in case plan A doesn't pan out. Your plan B may be to lease the property, live in it, or sell it for slightly less than you planned to sell it, but you should always have a plan B, because real estate transactions and markets are not always predictable.

Investigating the situation and the homeowners

The more you know about the homeowners and their situation, the better able you are to assist them in extricating themselves from their current predicament. Unfortunately, homeowners who are facing foreclosure often feel isolated, ashamed, resentful, and defensive. They may not be very forthcoming about the details that landed them in their current situation, and they may see you as merely an opportunist who is trying to sell their property out from under them.

In a way, they're right. You probably do want the property, and you want to make a profit. But that doesn't change the fact that the homeowners are trapped and need to explore their options. Your job at this stage is to convince the homeowners that they will see better results working with you than working with someone who's not quite on the level. In Chapter 9, I show you how to approach distressed homeowners and explain their options.

When you meet with homeowners, listen at least twice as much as you talk, and try to gather the information that can enable you to provide more valuable guidance and assistance:

- The total amount owed on the first mortgage and all other liens on the property, including any back taxes owed
- The current monthly payment on the house and on other outstanding loans
- The names and contact information for all lien holders — lenders, contractors, or others who have a claim on the property
- The amount of time before the property goes up for auction

- The value of any possessions the homeowners have that can be liquidated
- A list of any family members who may be able to help
- A clear idea of what the homeowners see as their options — sell the house, move to a rental unit, relocate, scale down to a smaller house

This brief list can start you on your information-gathering mission, but as you talk with the homeowners, other issues and opportunities often present themselves. Create a thorough record of your discussions with the homeowners so you can begin to paint a portrait of them in your mind. The more information you have, the more creative you can be in developing workable viable solutions. See Chapter 8 for additional details.

Setting and Sticking To Your Maximum Bid

Even the most cold and calculating real estate investors become enthusiastic about properties. They may fall in love with a particular house or simply get so caught up in the heat of an auction that they bid too much for a property. They then have to work twice as hard to make a profit on it.

REMEMBER

Before you bid on a property or make an offer to the homeowners, you should have a pretty clear idea of how much you can afford to pay for a property to earn the desired return on your investment — usually no less than 20 percent. Write down the amount and make a firm commitment to yourself to stick to it — bid or offer no more than your upper limit, no matter how hyped you become during the bidding or negotiations.

In Chapter 10, I show you how to set a maximum price for a property when preparing an offer to purchase directly from homeowners. In Chapter 11, I lead you through the process of preparing a maximum bid for an auction setting, and let you in on some strategies for effective bidding.

Taking Possession of the Property

When you buy a house, you usually expect to move into it on the agreed-upon date. You and the seller sign a purchase agreement in which the seller agrees to vacate the premises and turn over the keys on a specified date. Sometimes, the buyer requests possession at closing. In other cases, the seller agrees to move out one or two weeks later.

With foreclosures, the transfer of a property can be a long, drawn out, and messy affair. In some areas, you take immediate possession of a property as soon as you offer the winning bid and pay the trustee or courtroom clerk. In other cases, the homeowners retain possession of the property for the duration of the redemption period, which can last up to a year in some areas.

While you're waiting for the redemption period to expire, you may be tempted to start working on the house. Don't. You may invest $10,000 in renovations only to have the property owner decide to redeem the property just before you wrap up the project.

Even when the redemption period is over, you have no guarantee that the previous homeowners are going to quietly and orderly vacate the premises when their time runs out. In some cases, you can gently encourage the homeowners to move out. In other cases, you have to forcefully evict them, which is always a painful process for all parties.

In the following sections, I provide an overview of what to do to take formal ownership of a property and eventually take possession of it. In Chapter 16, I reveal your responsibilities as the new owner and cover the eviction process in more detail.

Completing the essential paperwork

When you purchase a property directly from the homeowners, you and the seller attend a closing in which a title company's agent or an attorney shuffle all the paperwork and file the necessary records.

When you purchase a property at an auction or sheriff's sale, however, you receive the deed, which you must then record at the Register of Deeds office to have your name officially added to the title. See Chapter 11 for details.

After dropping off the deed to have it recorded, make sure you obtain title insurance to protect you from any hidden claims against the property. Some title companies do not offer title insurance for foreclosure properties or properties you pick up at a sheriff's sale.

Paying property taxes and insurance

As soon as you purchase a property either from the homeowners or at an auction, you become the official owner of the property even though you may not be able to take immediate possession of it. As owner, you're in charge of insuring the property and paying property taxes:

- Call your insurance agent to obtain a homeowners insurance policy for the property.
- Pay the property taxes as soon as they're due. (You may need to pay back taxes when you purchase the property.)
- File an affidavit proving you paid the insurance and property taxes. If the homeowners decide to redeem the property, an affidavit enables you to recover any taxes and insurance payments you made during the redemption period.

See Chapter 16 for details concerning your responsibilities as a homeowner during the redemption period.

Convincing the current residents to move on

As the official owner and soon-to-be possessor of the property, your goal is to encourage the homeowners to move out without trashing the place or forcing you to evict them. You want the property broom clean and in the same condition it was in or better than when you first inspected it. The key to success in this area is to provide the homeowners an easy exit. Following are some suggested perks for assisting the homeowners out the door:

- Offer cash for keys and a nonredemption certificate — a signed agreement that the homeowners promise not to redeem the property.
- Provide a dumpster in which the homeowners can toss anything they don't want to move.
- Offer to pay for a moving van or pay a portion of their relocation costs.
- Offer to pay the first month's rent on a rental unit.

WARNING!

Don't hand over the cash until you get what you need. I've experienced several incidents in which homeowners took cash, agreed to move out, and then stayed put. Chapter 16 offers some additional suggestions along with instructions on how to evict homeowners who resist moving out.

Cashing Out: Realizing Your Profit

Assuming you purchase a property for the right price, you've already profited from it, but you don't see that profit until you cash out your chips. Various cash-out strategies are available, which I discuss in the chapters in Part V. The following sections provide a brief overview of your cash-out options.

Repairing and renovating the property to maximize its value

The most common way to cash out your profit is to repair and renovate the property and then place it back on the market in the shortest possible time. Time is of the essence, because every day you hold a property costs you — in monthly payments (if you financed the purchase), property taxes, insurance, and utilities.

The trick to repairing and renovating a property cost-effectively, as I explain in Chapter 17, is to plan well in advance and improve the property only enough to meet or slightly exceed the going price. Transforming a $150,000 property into a $250,000 property in a neighborhood where most homes sell for around $150,000 is a huge mistake. If buyers want a $250,000 house, they buy into a $250,000 neighborhood.

Marketing and selling to get top dollar

Your goal when selling a house is to sell it quickly at a price that's pretty close to its market value. To accomplish that goal, follow these marketing guidelines:

- **Set the price right the first time.** Don't set a super-high price hoping that the fish will bite. Your investment property is likely to linger on the market, during which time, holding costs continue to chip away at your profit. An asking price that's in line with comparably priced homes is best.
- **Get the word out through a successful real estate agent.** If you're thinking of saving money on real estate commissions by selling the house yourself, think again. Homes sell in about half the time and for more money through a real estate agent. What you may save in commissions, you end up losing through holding costs and by having to sell for a lower price.
- **Begin marketing as soon as you take possession.** Marketing begins as soon as you begin your renovations, especially if you start renovating the exterior first. Neighbors notice and begin to gossip, and word-of-mouth advertising begins to take off.
- **Plant a For Sale sign on the front lawn when renovations are nearing completion.** A For Sale sign removes all doubt that the house is for sale.
- **Stage the house impeccably.** Clean and scrub inside and out, mow the lawn, freshen up the landscape, remove the clutter, tastefully furnish and decorate the interior, set out some fresh bouquets of flowers, and let the buyers stream in.

For additional tips and strategies to sell your property quickly and for top dollar, check out Chapter 19.

Cashing out equity by refinancing

When you purchase a property for less than its market value, you automatically have equity in the property. Renovations to bring the property up to its market value add more equity.

You can cash out the equity by refinancing it for more than you paid for it to realize your profit almost immediately. Keep in mind, however, that by refinancing for more than the purchase price, you take on a larger mortgage, and the increased interest chips away at your total profit over time. Refinancing does, however, provide you with capital to fuel your next investment or to pay for additional renovations.

For more about refinancing to cash out equity, skip to Chapter 19.

Profiting in other ways

Selling and refinancing are two of the quickest and most common ways to realize the profit from foreclosures, but other strategies are also available:

- Negotiate a short sale. (See Chapter 15.)
- Lease the property. (See Chapter 18.)
- Lease the property back to its previous owners. (See Chapter 19.)
- Sell the property to the homeowners' family members. (See Chapter 19.)
- Sell your position in the property to another lien holder. (See Chapter 19.)

Chapter 2

Getting Up to Speed on the Foreclosure Process

In This Chapter

- Brushing up on the differences in how foreclosures are handled
- Investigating the early missed payment pre-foreclosure period
- Finding opportunities in the Notice of Default stage
- Arriving at the foreclosure auction stage
- Waiting out post-foreclosure, from redemption to eviction

A common foreclosure myth is that it's a one-time event. Homeowners miss a mortgage payment or two, and the lender swoops in and scoops up the property. The fact is that foreclosure is typically a long, drawn-out legal process that begins with missed payments, proceeds through some sort of legal system, and often results in homeowners losing their homes.

An understanding of the foreclosure process reveals the various stages at which you can purchase properties. By knowing what to expect, you can often diminish disappointment and maximize your opportunities.

This chapter provides a roadmap of the foreclosure process beginning with some notice to the homeowners and the public of missed mortgage payments and ending with the homeowners relinquishing possession of the property. Anywhere along the way, the homeowner has options to interrupt the process and regain control of the property. I point out these opportunities so you can better assist homeowners in making choices and to give you a heads up of what a homeowner can do to derail your purchase plans.

TIP

Homeowners find themselves facing foreclosure for any number of reasons, including long-term illness or disability, overspending, substance abuse, divorce, and gambling, to mention only a few. As a real estate investor, you gain nothing by judging people in foreclosure. The best way to approach homeowners in foreclosure is with respect and empathy. By enabling homeowners to put the past behind them and establish a more solid financial footing, you may place them on a more productive path.

Identifying the Foreclosure Process in Your Area

The end result of foreclosure is that the homeowners lose ownership and ultimately lose possession of their property. That's true no matter where you're buying foreclosure properties. However, different states and counties follow different foreclosure procedures. The two main procedures are:

- Foreclosure by trustee sale or *foreclosure by advertisement*
- Foreclosure by judicial sale or *judicial foreclosure*

The following sections describe these two types of foreclosure. To find out which process your state follows, check the appendix at the back of this book. Counties may also have their own local rules for how the sale is actually carried out, so visit your county courthouse (the Register of Deeds office), and ask them to explain the rules and regulations. I also recommend that you sit in on a few auctions before bidding on anything.

Foreclosure by trustee sale

A few more than half the states follow the trustee style route. When the homeowners purchase a property in one of these states, the county issues a sheriff's deed that the trustee (which may be the sheriff in some areas) holds in trust until the mortgage is paid in full. After paying off the mortgage, the trustee releases the deed to the homeowners.

If the homeowners default on the payment, the lender can notify the trustee to initiate foreclosure proceedings. The trustee can then sell the property and transfer proceeds to the lender as payment of the loan. Because the foreclosure does not need to progress through the courts, foreclosure by trustee sale is typically much faster than foreclosure by judicial sale.

Foreclosure by judicial sale

Fewer than half the states follow a judicial foreclosure process. As you've probably guessed, judicial foreclosure passes through the justice system — the state (circuit court) or district court. When the homeowners default on their mortgage, the lender files a claim to recover the unpaid balance of the loan from the borrowers. The courts decide the case, which typically takes a long time to resolve — typically 4 to 6 months, but sometimes up to a year. During this time, unless the homeowners work out a payment plan or some other solution with the lender, they're almost guaranteed to lose their home.

Exploring the Missed-Payment Notice Stage

Some lenders initiate foreclosure proceedings as soon as the homeowners miss one or two payments. Other lenders start sending reminder notices, often following a predictable timeline:

- **Two-week notice:** Some lenders give homeowners a two-week grace period, after which they begin to start calling the homeowners or sending them letters.
- **30-day notice:** When a payment is so late that it's time for the next payment, the lender gets a little jittery and ramps up its efforts. The lender may even begin levying late payment fees.
- **45-to-60 days' notice:** Unless the homeowners contact the lender and work out some new payment agreement, the lender typically sends out a certified letter insisting that the homeowners pay up.
- **90-day limit:** If the homeowners still have not contacted the lender or shown any commitment to make good on the loan, the lender typically initiates formal foreclosure proceedings. At this point, the lender transfers the matter to outside legal counsel (an attorney), and the attorney in charge has a foreclosure notice (sometimes referred to as an NOD or Notice of Default) posted. Once the attorney starts foreclosure by advertisement, these legal notices or advertisements attract the investors.

REMEMBER

The missed-payment notice stage, prior to the start of foreclosure proceedings, is the best time for homeowners to act and the best time for you to step in to assist them. In 90 percent or more of the foreclosures I've been involved in, the homeowners' best option is to sell the property, cut their losses, and find more affordable housing. With your assistance, the homeowners still have time at this stage to take advantage of this option.

Getting Serious: The Notice of Default

For investors, the foreclosure process officially kicks off with the posting of the Notice of Default (NOD) or foreclosure notice in the county's legal newspaper or the local newspaper — private, for-profit publications that get the word out to prospective bidders. At this point, the distressed homeowners usually realize the inevitability of losing their property. Some remain in denial while others become resigned to the fact, even though they may have several options to abort the foreclosure process and regain control of their property . . . and their finances.

TIP

If you plan on purchasing properties prior to the foreclosure sale, your best chance is to contact the homeowners before the NOD is posted. After the NOD appears in the papers or in legal publications, competition for the property begins to heat up. The only way to find distressed homeowners before the NOD is posted is through word-of-mouth networking. See Chapter 3 for additional guidance on choosing the stage of the foreclosure process that's right for you, and refer to Chapter 6 for word-of-mouth networking tips.

Proceeding to the Foreclosure Sale

Prior to the foreclosure sale, the homeowners can work with the lender or their attorney to delay or cancel the foreclosure sale. In other words, just because you see a foreclosure notice in the local paper doesn't mean that if you show up for the sale, that property is going to be auctioned off.

TIP

Calling the attorney in charge of the foreclosure prior to the sale is a great way to find out if the property is going to be offered at the sale. The attorney's name is usually listed on the foreclosure notice. In Chapter 7, I show you how to pick out important details on the foreclosure notice.

At the foreclosure sale, you have an opportunity to bid against other investors for any properties being auctioned off. As I explain in Chapter 11, some auctions have open bidding, whereas others use a sealed bid system. However your county chooses to hold its auctions, a few words of advice can assist you in acquiring properties and not losing your shirt:

- Sit in on at least five auctions before bidding to get a feel for the process and gather information.
- Research the property thoroughly before you bid. In Chapter 8, I show you how to build a file for each property packed with useful details.
- Buy only senior liens (first mortgages). You can really get burned buying junior liens because foreclosure typically wipes these off the books. When you have more experience and knowledge, you can start working the junior lien circuit and tax liens as I discuss in Chapter 15.
- Set a maximum bid and never ever exceed that amount, no matter how juiced up you get at the auction. See Chapter 11 for details on how to calculate your maximum bid.
- When you plan to bid, show up with a cashier's check. Most auctions require payment at time of purchase or within an hour. For additional information on paying for a property after the auction, check out Chapter 11.

Halting the Foreclosure Process

Distressed homeowners are plagued by a swarm of emotions ranging from disbelief and resentment to shame and guilt. They may have several options to stop the foreclosure process, but they're too upset and confused to think clearly or explore their options and so angry or fearful that they hesitate to contact the lender in order to work out a solution.

In the following sections, I introduce various ways that homeowners in foreclosure can stop or delay the foreclosure process. Use this information not only to better assist distressed homeowners, but also to prepare yourself for the possibility that the homeowners may choose to cut you out of a promising deal by successfully negotiating with the lender or another investor.

Encourage the homeowners to contact their lender, even if this results in you losing a prospective property. Never supply misleading information to discourage homeowners from taking the action that's best for them. Be a real estate investor, not a con artist. In addition keeping you out of legal trouble, acting with integrity establishes goodwill with the homeowners and leads to future referrals, as I point out in greater detail in Chapter 22.

Reinstating the mortgage

Prior to the foreclosure auction, homeowners who can get their hands on enough cash may have the option of *reinstating the mortgage.* This consists of making up for all missed payments and paying any late fees or other penalties.

To reinstate the mortgage, the homeowners must contact the lender prior to the auction date to verify that reinstatement is an option. If the option is available, the homeowners must then work out a payment schedule with their lender.

If you're trying to assist distressed homeowners in finding a solution, and you're running out of time, the homeowners can file for bankruptcy to buy more time. See "Filing for bankruptcy," later in this chapter for details.

Requesting and receiving a forbearance

When homeowners have a temporary loss of income with the promise of regaining their financial footing, the lender may agree to a *forbearance,* in which the homeowners can delay payment for a short period or negotiate a payment plan to make up for missed payments over the course of several months, as explained in the following section.

A smooth operator

I once purchased a property at a sheriff sale and did everything I could to contact the homeowner. I even tried to drop in on the homeowner, but she slammed the door in my face as though she knew who I was and had been expecting me.

Later, I discovered that a con artist, Brian, had gotten to her during the redemption period. He established some sort of emotional connection with the homeowner, took her to the county building to pick up the overbid (the money I paid for the property at auction in excess of what was owed on it), and convinced her that he could save her house for her.

Brian bought her a vacuum cleaner and a few groceries for her signature on a *quit claim deed* — a document signing away her rights to the property. He videotaped her making statements that he thought would protect him in the court of law.

With quit claim deed in hand, Brian redeemed the property, and I got my money back. Brian then sold the property to an investor named Ray. Ray came to my office, and I, without knowing what had transpired, bought the property and sold it to another investor. When that investor showed up at the homeowner's house to work out some rental agreement with her, he learned about the con job and wanted nothing to do with the property.

Eventually, the matter wound up in court. I bought back the property and gave the homeowner some money so she could move to a more affordable home. While in court, I got a $100,000 judgment against Brian. Last I heard, Brian was scheduled for a creditors hearing.

Never take advantage of homeowners for your own benefit. After all, this is their home, and any equity they have in that home is theirs. Commit to becoming a champion of the homeowners. If you can help and earn some payment for your assistance, everybody wins. Quick money never lasts. By acting with integrity and in the best interest of the homeowners, you provide a much-needed service to a suffering portion of your community.

The lender may also offer some sort of combination between a forbearance and reinstatement, enabling homeowners to delay payment for a short period and then bring their payments current by a specific date.

TIP

The phone number on the mortgage payment coupons may put you in contact with the loan servicer who processes the payments instead of the lender who actually owns the loan. The loan servicer may not offer much assistance, so ask the loan servicer who the lender is, and contact the lender directly.

Mortgage modification or repayment plan

To enable financially strapped homeowners to slowly make up missed payments, a lender may agree to a mortgage modification or repayment plan:

- A *mortgage modification* consists of adding the past-due payments and penalties to the remaining principal, so the homeowners pay off the past-due amounts and penalties over the life of the loan. This arrangement is commonly known as "adding amounts due to the back of the loan."
- A repayment plan enables the homeowners to submit payment of a portion of their past-due amount and penalties with future payments until the past-due amount and penalties are paid off.

When homeowners are already having trouble making their monthly mortgage payments and do not have the resources to cover higher payments, mortgage modification and repayment plans are rarely ideal solutions. These options often simply delay the inevitable.

Filing for bankruptcy

Filing for bankruptcy sounds like a permanent solution to any significant financial predicament like foreclosure, but it's not the ideal solution. It destroys the homeowner's credit rating for seven years or so and doesn't exactly wipe all debt off the books. Bankruptcy simply relieves some of the debt burden and provides homeowners some extra time to restructure their remaining debt.

Bankruptcy, however, is one more option for distressed homeowners, and it's certainly something you should know about as an investor in foreclosures. By filing for bankruptcy, at least a couple of days before the auction date, a homeowner can delay the foreclosure process and leave a property you already purchased in limbo — at least until the foreclosure trustee and the courts sort out all the legal issues.

TIP

Bankruptcy is another opportunity for real estate investors. As the trustee or courts decide how to liquidate the property, you may be able to step in and work with the lawyers and trustee to purchase the property and make their lives a little easier. Chapter 14 shows you how to acquire properties in bankruptcy.

Agreeing to a "deed in lieu of foreclosure"

When homeowners have very little to none or even negative equity built up in their property and they have no hope of turning the financial tide, they may offer the lender a *deed in lieu of foreclosure.* The homeowners agree to pass the deed and their house keys to the lender without having to go through a messy public foreclosure process.

Although this may provide the homeowners with a less embarrassing escape route, it often leaves the lender with a property that the lender doesn't want along with the expense of repairing and rehabbing the property and selling it. As an investor, you may be able to step in as the ultimate middleman, negotiate with the lender, getting it to accept less than the full loan amount due (what real estate insiders call a *short sale*), and still provide the homeowner with a clear escape route.

Some investors around the country make a really good living just working short sales. If you can't purchase a foreclosure property for a low enough price to make a profit, negotiating a short sale can make the deal more profitable. Keep in mind, however, that lenders won't agree to short sales if they foresee the homeowners walking away with money, and you shouldn't negotiate a lower payoff to put money in the pockets of the homeowners. See Chapter 15 for details.

Getting one last chance during the redemption period

Any reasonable person would assume that when he buys a property at a foreclosure sale, it's automatically his property, but that's not always the case. Many areas of the country have a mandatory redemption period, which can last from a few months to an entire year. Check out the appendix at the back of this book to find out about the redemption period in your area.

During the redemption period, the person who purchased the property at the sale gets to insure the property and pay the property taxes, but the foreclosed-upon homeowners have the right to redeem the property. To do so, the homeowners have to come up with enough cash to pay off the mortgage in full along with any interest and penalties.

Depending on the rules that govern redemption in your area, the buyer may or may not have the right to recover expenses (including property taxes and insurance) from the homeowners. Consult your real estate attorney.

If you purchase a property at a foreclosure sale in an area that has a mandatory redemption period, about 50 percent of the time you end up with the property. The only sure way you end up with the property is in markets that don't have redemption periods. (Check out the appendix at the back of the book to determine whether your state has a mandatory redemption period.) To protect your investment in areas that have a redemption period, take the following precautions:

- If possible, repair any defects in the house that may be considered unsafe or lead to further deterioration of the property. If the property is vacant and unsafe, and you don't take care of the problem immediately, the property is likely to lose value. Avoid investing any more money in repairs than is absolutely necessary — if someone redeems the property, you stand to lose that money.
- Insure the house, and file an affidavit of payment, so if the homeowners redeem the property, you may be able to recoup your expenses. Consult your real estate attorney to determine your rights to recover expenses.
- Pay the property taxes, and file an affidavit proving payment.
- Don't invest in any renovations, just in case the homeowners do redeem the property. You could lose all the money you invested in the renovations. Generally you perform repairs only to protect your investment if the house is vacant or if you've worked it out with the occupant. Different states may have different abandonment laws which may restrict you from doing anything. Your real estate attorney can provide guidance here.
- Keep an eye on the property to protect it from vandalism and theft. Some disgruntled homeowners may strip the property before vacating it.

For additional advice on how to survive the redemption period, see Chapter 16.

TIP

All sales are not final in areas with redemption periods. If you miss out on an opportunity during the foreclosure sale, you haven't necessarily lost the property for good. The homeowners still control the property, and you can work with them to bump the investor who purchased the property out of the deal. See Chapter 11 for details. Of course, the knife cuts both ways — you could end up getting bumped. You get your money back, but you lose out on the property.

Losing out on a junior lien

I bought a first mortgage (senior lien) at the first foreclosure sale on a property for $25,000. Another investor bought the second mortgage (junior lien) for $25,000. Thinking that he had the property in the bag, he spent another $25,000 during the redemption period renovating the house, so now he had $50,000 invested in a property that was worth about $100,000.

Sounds like a good deal, but the investor made a huge mistake — he failed to pay off the senior lien, which I held. He could have redeemed the $25,000 senior lien that I held, sold the property for $100,000, and made a $25,000 profit, but he forgot to redeem the senior lien.

I took possession of the house and put it up for sale. The other investor called all upset because he was convinced that the house was his. I had to explain that due to his oversight, the house was not, in fact, his, but mine.

The moral of the story is that if you buy a junior lien attempting to control the senior lien, remember to redeem that senior lien.

Finalizing the Foreclosure: Ushering the Previous Owners Out the Door

Eviction is an unpleasant experience for both the evictor and the evictee, so you want to do everything you can, within reason, to encourage the previous homeowners to voluntarily vacate. Offer them an incentive package — a free dumpster, use of a moving van, relocation expenses, or whatever they need — to put this problem behind them and move on to a potentially rosier future.

If that doesn't work, you have no option but to file a request with the district court to have the homeowners evicted. Once you file your request, assuming it's approved, the sheriff's office delivers the homeowners an eviction notice stating the date on which the eviction will occur. On that date, if the homeowners haven't vacated the premises, the sheriff shows up and forcefully removes the homeowners and their belongings, and you formally take possession of the property.

Putting some empathy in eviction

I knew an investor who reveled in evictions. He would drive to the eviction and park his red Porsche out in front of the house and make fun of the people being evicted. He even went so far as to take photographs and hang them on his office wall. The company he worked for was doing a billion dollars' worth of business annually, so maybe that made this cold-hearted investor feel justified, but the only real justice was what finally happened to him and all the senior management at his company.

The Security and Exchange Commission investigated their business practices and found them guilty of several counts of mortgage fraud. The investor is now serving a four-year sentence in a federal prison.

When you have to evict homeowners, do it with heart. Put yourself in their shoes and try to appreciate how you would feel in a similar situation or how you would feel if that was one of your family members being evicted. If possible, rent a moving truck for the homeowners and help them pack and load their possessions. Whatever you do, don't cause additional pain along with getting your gain.

Chapter 3

Picking Your Point of Entry in the Foreclosure Process

In This Chapter

- Buying directly from homeowners in pre-auction
- Chasing foreclosure notices: pros and cons
- Scoping out properties at foreclosure auctions
- Tracking down bank- and government-owned properties

Foreclosure investing encompasses much more than simply buying properties for pennies on the dollar at a foreclosure auction. The foreclosure process often takes three months to a year to run its course, and investors can step into the process at any time to scoop up a property. In fact, investors can even step in before official foreclosure proceedings begin and in some areas months after they wrap up.

TIP

Although you can buy properties at numerous stages in the foreclosure process, I recommend that you become a specialist in one area first. Focus on pre-auction properties, auctions, or post-auctions, so you can become an expert in one area. You can branch out later, as you become more experienced, develop better connections, and strengthen your investment team and your financial position.

In this chapter, I reveal the various entry points in the foreclosure process, covering everything from pre-auction to post-redemption, also known as REO (Real Estate Owned) opportunities. I point out the pros and cons of investing at each stage, so you can make a well-informed decision of where you'd like to begin your journey in foreclosure investing.

Dipping In at the Pre-Auction Stage

Homeowners often feel reluctant to take action when they first get an inkling of financial foreboding. Instead of contacting their lenders, an attorney, or a real estate agent who specializes in foreclosures to seek advice and try to work out a solution, they often stick their heads in the sand and hope the problem goes away. By the time they act, they're usually too late. Behind on their house payments, drowning in credit card debt, and unable to pay back taxes, their fate is sealed months before the bank initiates foreclosure proceedings.

When the bank finally moves forward to foreclose, the homeowners are often in a panic. They don't know what to do or where to go for reliable information. As a foreclosure investor, you can step into the process, provide homeowners with options to cut their losses, and perhaps even assist in enabling the homeowners to retain possession of their property.

TIP

You may think that doing everything you can to enable homeowners to retain possession of their property is contrary to the idea of profiting from foreclosures. In about 90 percent of pre-auction foreclosures, however, the homeowners are too deep in debt and must sell their home. By acting with integrity, you give yourself a much better chance of obtaining the property . . . and doing some good at the same time. See Chapter 21 for specific ways you can assist distressed homeowners.

Exploring the pros and cons of pre-auction foreclosures

Although you can certainly wait for the foreclosure auction to roll around, the pre-auction stage offers several benefits to foreclosure investors:

- Less competition from other investors.
- More options for negotiating deals with homeowners and their lenders.
- More time to put together a deal and close on the house.
- Increased opportunity to inspect the condition of the house, inside and out.
- No redemption period or other legal issues at the end that can sink the deal. Once you close on the property, it's yours. You may have to wait a week or two to take possession, depending on your agreement with the homeowners, but you don't have to wait three months to a year for the redemption period to expire. For more about redemption, skip to the section near the end of this chapter called "Waiting Out the Redemption Period — If Necessary."

At this point, you're probably ready to dive into the pre-auction stage and start scooping up properties from homeowners eager to shed the financial burden. Before you leap, consider some of the following drawbacks of buying directly from homeowners:

- Emotional fallout, including anger and resentment, from the loss of a home
- Complications of dealing with other people's financial messes
- Misleading information or outright lies from homeowners who are still in denial
- Indecisiveness of homeowners who change their minds at the last minute because they really don't know what they want
- Legal issues of just how far you can go to convince homeowners to sell their property at less than market value

Carefully consider the pros and cons before investing in anything and honestly assess your ability to deal with the negative aspects of certain investment options. Buying foreclosure properties in the pre-auction stage isn't for everyone.

Guiding homeowners to good decisions

When helping homeowners, you can't try to pass yourself off as an attorney, accountant, financial advisor, or therapist, unless you really are one. However, you're often called on to play some of these roles. Like a therapist, you have to learn to listen to the homeowners. Like an accountant, you need to be able to look at the homeowners' finances to assess their options. And, like an attorney, you need to know the foreclosure and redemption laws in your area.

WARNING!

Make it very clear to the homeowners that you are not an attorney, real estate agent, or accountant, unless you really are one. State up front that you're an investor representing yourself. Full disclosure is the best policy. Passing yourself off as something you're not is fraud.

REMEMBER

You cannot offer legal advice if you're not a licensed lawyer, but you can inform homeowners of their options and recommend professionals who can help. If the homeowners can refinance their way out of a foreclosure, you may be able to steer them to a loan officer or financial advisor who can provide additional assistance. In Chapter 4, I show you how to assemble a team of experts to assist you in buying and selling foreclosure properties, so you should have plenty of experts on hand to recommend to the homeowners.

A typical day in the foreclosure office

As a real estate broker, I once met with a couple facing foreclosure. The husband worked two jobs, and the wife took care of the bills. Though he was working hard to make ends meet, the couple had fallen behind in their mortgage payments and were receiving notices from their lender. We set up a meeting at my office to do a conference call with the lender to work out a possible solution.

When the couple arrived at my office, I immediately saw the nature of the problem. The wife was decked out in designer clothes and adorned in jewelry that would have made the Queen of England jealous.

After looking over their finances, I explained that in order to avoid foreclosure, the couple would need to slash expenses and sell some of their more valuable assets.

Upon hearing my words, the wife was visibly upset. Angry and near tears, she stood up and said, "What do you want me to do . . . take the clothes off my back and the rings off my fingers?!"

I said, "You can leave your clothes on, but let's take a closer look at those rings." The couple was $10,000 behind on their mortgage payments. I agreed to take the jewelry and give them $10,000 in return, so they could sell the house and move on. The next day, I took the jewelry to a friend of mine who owned a jewelry store. He appraised the rings at $5,000. So, I ended up taking a $5,000 loss, but I scored a great Valentine's Day gift for my wife!

Dealing with anger and angst

Understandably, when people are in a financial bind, they're often upset, anxious, and angry. Parents have the daunting task of facing their kids and telling them, "We can no longer afford to live here." They're embarrassed about what their neighbors, friends, and family may think. They may be angry at their boss for laying them off or firing them. In many cases, the husband or wife has just found out about the pending foreclosure from their significant other who spent the family into the poorhouse.

When you show up at the home of a couple or individual facing foreclosure, and you tell the homeowners that you want to help them by buying their property, all that rage is likely to get unleashed on you. Even if you can manage to avoid direct conflict, you may very well end up refereeing a domestic dispute or witnessing emotional outpourings that you're just not used to seeing.

Distressed homeowners are often most upset about something that happened in the past — something that they can't go back in time and fix. One of your first jobs when dealing directly with homeowners is to encourage them to put the past behind them and address the current situation. This takes a lot of steam out of anger over the past. See Chapter 9 for more tips on defusing potentially explosive situations.

You can often relieve some of the pain of foreclosure by letting the homeowners know that they're not alone. Know the foreclosure statistics for your area, and share this information with them along with letting them know about their options. This can often defuse a tense situation and remove some of the anger that may be causing a rift in a couple's relationship. Ask at your county's Register of Deeds office — sometimes they track foreclosure numbers for the county and may be able to quote state statistics.

Assessing your ability to deal with pre-auction scenarios

The most successful pre-auction investors are people who are well versed on local foreclosure laws and procedures and who can quickly and accurately assess the average homeowner's financial predicament. To determine if you have the qualities to successfully invest in properties in the pre-auction stage, place a checkmark next to any of the following statements that you feel are true:

- ❏ People generally like me and trust me right off the bat.
- ❏ I feel comfortable talking with people I've never met.
- ❏ I'm a good listener.
- ❏ I'm diplomatic, often acting as the mediator when friends, family members, or co-workers have issues with one another.
- ❏ I never met a problem I couldn't solve.
- ❏ I'm good with math, especially dollars and cents.
- ❏ I can tell people the truth even when they don't really want to hear it.
- ❏ I can handle disappointment. Even if I've invested a great deal of time and effort in helping a homeowner, I won't get terribly upset if I don't get the house.
- ❏ I can let people fail, even after I offer them outstanding advice on how to avoid a catastrophe.

Having every single one of these qualities is not essential for success in investing in pre-auction properties, but if you checked only two or three items, you may want to consider stepping into the foreclosure process at the auction or post-auction stage. The more of these qualities you have, the more successful you may be in dealing directly with the homeowners.

Pursuing Foreclosure Notices

Whether you buy properties directly from homeowners prior to the auction or wait until the auction stage, the weekly foreclosure notices in your area are required reading. In almost all areas of the country, the lender must post a weekly foreclosure notice or Notice of Default (NOD) in a publicly accessible publication several weeks prior to the auction. In my area, the foreclosure notice must be posted for four consecutive weeks prior to the sale in any public newspaper that serves the area. The appendix at the back of this book explains each state's requirements for posting foreclosure notices.

The posting of the foreclosure notice is almost an entirely separate stage of the foreclosure process — after negotiations between the homeowners and lender break down, but before the property is sold at auction. At this stage, every foreclosure investor in your area probably knows about the property, and any investors interested in buying the property prior to auction are likely in the process of trying to contact the homeowners.

The investor who arrives first and whom the homeowners trust most is typically the investor who stands to get the property.

TIP

As you discover in Chapter 7, you can find foreclosure properties even before the foreclosure notice is posted by keeping your ears open, networking effectively, as explained in Chapter 6, and getting the word out that you buy properties.

Knowing the benefits of waiting for the foreclosure notice

Many foreclosure investors don't like dealing with distressed homeowners until the official foreclosure notice is posted because until that point, homeowners may be unwilling to accept the fact that foreclosure is imminent. The posting of the foreclosure notice removes most of the lingering doubt and acts as a wakeup call for the homeowners to take action.

The foreclosure notice offers several additional benefits:

- Contains the location of the property (usually a legal address, not a mailing address, but you can use the legal address to obtain the mailing address, as discussed in Chapter 11)

- Lists the names of the homeowners being foreclosed upon, so you can refer to them by name, instead of addressing them as Dear Sir or Madam
- Specifies the name of the lender foreclosing on the property, so you have the information you need to gather more information from the lender
- Provides the name of the attorney or trustee in charge of liquidating the property, so you have someone to call for additional details

As you learn throughout your experience as a foreclosure investor, every bit of information you have about a property is a valuable puzzle piece that clarifies the situation and enables you to put together an attractive deal that benefits all those involved.

REMEMBER

Just because the lender posts a foreclosure notice does not mean that the property is destined for the auction block. Any time prior to the sale, the homeowners can strike a deal with the lender or refinance to call off the foreclosure or strike a deal with an investor to sell the property. As soon as the foreclosure notice is posted, the clock starts ticking for any investor looking to buy the property prior to auction.

TIP

Keep track of properties from the day they're advertised to the time they're sold. Very often, a particular foreclosure sale is adjourned, so the property doesn't go up for auction on the scheduled day. By following the adjournments, you often find that the property goes up for sale later. If you're prepared, you may be able to grab the property without any competing bids.

Weighing the drawbacks of waiting for the foreclosure notice

Although the posting of the foreclosure notice delivers some valuable benefits to foreclosure investors, it also heats up competition among area investors who are all looking for the best deals in the area. As soon as that foreclosure notice is published, every foreclosure investor working the pre-auction circuit catches the scent and heads out to research the property and contact the homeowners.

REMEMBER

When buying properties from distressed homeowners prior to auction, finding out about prospective foreclosure properties prior to the posting of the notice often gives you a competitive edge. Networking, as discussed in Chapter 6, provides the earliest leads. Reading the notices as soon as they're posted and acting quickly to contact the homeowners is the next best option.

Wrapping up your deal before the sale

Buying a property from the homeowners prior to the sale is a standard seller-to-buyer transaction. If you've ever bought a house (you should be a homeowner if you're investing in real estate), then you know the drill:

1. **Present your offer to the homeowners in the form of a purchase agreement.** You may need to work through a series of counteroffers to agree on a price and terms.
2. **Have the property professionally inspected.**
3. **Order title insurance to protect yourself if the title has any hidden claims against it.**
4. **Sign the papers at closing.**
5. **Take possession of the property on the agreed-upon date.**

REMEMBER

Because you purchased the property directly from the homeowners, they have no right of redemption, so you don't have to wait around for several months. You can immediately move into the property, renovate and sell it, or turn it into a rental unit. Refer to Part V for more details about profiting from a property after you take possession of it.

Bidding for a Property at a Foreclosure Auction

Foreclosure investors often choose to do their bidding at auctions. A common misconception about foreclosure auctions is that investors bid on properties. The truth is that investors bid on mortgages (also called liens). What's the difference? When you buy a property from homeowners, you own the property. When you buy a lien at a foreclosure sale, you may or may not eventually take possession of the property — if your area has a redemption period, the homeowners or someone else who has a legal claim to the property can redeem it. Check the appendix at the back of this book and consult your county's Register of Deeds office to find out more about the redemption period in your state.

For a better understanding of what you're actually buying at a foreclosure auction, brush up on the following types of liens:

- **Senior lien:** The senior lien or *first mortgage* is the loan that the homeowners took out to purchase the property. I recommend that novice investors always buy first mortgages, because owning the senior lien gives you the best opportunity to eventually take possession of the property.
- **Junior lien:** The junior lien is any other loan the homeowners took out using their home as collateral. A junior lien is usually a second mortgage, but it can be a home equity loan or contractor financing provided for home improvements. Junior liens are often wiped off the books during the foreclosure process, so they are often very risky investments.
- **Tax lien:** A tax lien is a claim against the property for unpaid tax bills. Unlike junior liens that foreclosure typically erases, a tax lien remains in place after foreclosure. If the tax lien is for overdue property taxes, the buyer must pay the taxes. If the lien is for income taxes, the IRS or other taxing agency may choose to forgive the taxes, but make sure the foreclosing attorney notifies the IRS, as explained in Chapter 11. Buying a property tax lien is usually a safe investment, because if someone else purchases the property, you stand to get your money back and perhaps even earn a little profit. For more about profiting from tax liens, see Chapter 15.

Standing afar from the maddening crowd

I always recommend that first-time foreclosure investors sit in at least five auctions before bidding. This gives you a feel for the auction process, enables you to identify the players in your neighborhood, and can often lead to connections that may pay future dividends.

When you begin sitting in on auctions, you're likely to notice the same people showing up week after week, a majority of whom never bid on properties. Some people attend for the entertainment value, and that's fine, but others consider themselves the resident foreclosure experts. A new face in the crowd draws their attention, and they offer what they're convinced is solid investment advice.

Steer clear of these foreclosure investor phonies. You can be nice, smile, and exchange the usual pleasantries, but the majority of the hand-sitters at foreclosure auctions who actively pursue you to bend your ear are either doing so for attention or to sell you a bill of goods — an investment property that they got stuck with.

The people you want to seek advice from are the people showing up every week, bidding on properties, buying them, and turning them over for a profit. Unfortunately, these knowledgeable individuals aren't likely to share their wisdom with a novice investor looking to compete against them. If you can earn their trust and offer something of value in exchange, they may be willing to pass along some advice, but don't hold your breath.

Don't bid at auctions until you fully understand the process and know what you're buying. Whenever a foreclosure guru stages a foreclosure seminar in my area, my office begins receiving calls from angry novice investors who purchased junior liens thinking they were buying senior liens. One investor purchased over $100,000 in junior liens only to find out later that these liens were useless pieces of paper. Chapter 11 shows you how to prepare for an auction well in advance.

Weighing the pros and cons of buying at auctions

The foreclosure auction provides you with an opportunity to purchase a controlling interest in the property without having to deal directly with the homeowners in often emotional and ugly situations. In a way, the auction simplifies the process of acquiring properties. You show up, submit the winning bid, and walk away with the sheriff's deed.

Buying at auction, however, presents several additional challenges, including the following:

- You may not have the opportunity to thoroughly inspect the property, although you should at least inspect the property from the outside, as I advise in Chapter 8.
- Properties are often sold as is, so you're more likely to take possession of a property that requires costly repairs.
- Cash payment is usually required at the time of purchase, so you need to show up with cashiers check. In some cases, you have a few hours or days to come up with the cash, but you still need ready access to cash to close on the deal.
- Depending on the number of investors at the auction who actually bid on properties, you may face some stiff competition.
- When you buy a property at an auction in an area that has a mandatory redemption period, you may need sufficient funds to hold the property for several months to a year until you see your profit. (If you're using your own money, you need just enough cash to insure the house and pay the property taxes. If you borrowed the money, you may need additional cash to cover the monthly payments. For more about financing your purchase, refer to Chapter 5.)

REMEMBER

Throughout this book, but especially in Chapters 10 and 11, I reveal tips and techniques for meeting these challenges and minimizing your risks of bidding at auctions. Only by being thoroughly prepared going into an auction can you confidently purchase properties that are almost sure to turn a profit.

Setting a maximum bid well in advance

One big mistake to avoid at an auction is getting caught up in the excitement of the bidding experience. I know the risks of overbidding firsthand, because I have trouble restraining myself at auctions. I hate to lose, so if someone's bidding against me, I always win — the bid, that is. Only later do I realize that my obsession with winning made me the big loser for having spent too much for a property.

TIP

The trick to effective bidding is to research the property thoroughly and set the highest price you can afford to pay for the property and still make a profit of 20 percent or more. That's your ceiling. You can bump your head on it, but don't crash your head through it, or you will have serious headaches in the future. For auction bidding tips and tricks, see Chapter 11.

Putting on your poker face

Bidding on a property at foreclosure is a bit like sitting around a poker table and trying to figure out why a particular investor is bidding on a specific property for a certain amount of money. In some cases, the other investor may know more about the property than you do. In other cases, the investor knows less. The person may be bidding on instinct to drive up bidding or simply to toy with other investors.

The comparison of bidding on foreclosure properties to playing poker, however, ends there. Bidding on properties is a high-stakes game in which you stand to lose as much or even more than you stand to gain. You may never know why a particular investor bids a specific amount on the property, but you always need to know why you're bidding a specific amount, what you're bidding on, and how high you're willing to bid.

With a fully fleshed-out property dossier, which I show you how to assemble in Chapter 8, you hold all the cards in the deck. This enables you to put on the dispassionate poker face required to win the bidding game. You know exactly how much you can afford to bid to earn the desired profit. Not everyone who's bidding against you will have the same advantage.

Acquiring Properties after the Auction

The auction close doesn't signal the end of your opportunity to acquire foreclosure properties. For investors who choose to focus on post-auction properties, an auction's close signals the beginning. These investors don't want to deal directly with homeowners, and they prefer to avoid the sometimes messy auction process. They'd rather buy properties from the new owners.

In the following sections, I list various opportunities and resources for tracking down post-auction properties, from bank-owned and government-owned repos to properties that have been seized because they were paid for with ill-gotten gains. You can make a good profit by focusing on any one of the categories I describe.

The opening bid at an auction is typically the amount owed on the property, plus attorney fees, plus a dollar. Contrary to what many people think, banks don't want to be in the real estate business, so they rarely bid up a property in order to take possession of it. A bank holding a second lien may, however, bid on the first lien to protect the bank's interest.

Scoping out REO properties

Auctions typically start out with a minimum bid. If nobody in the room bids high enough, a representative for the bank that's foreclosing offers a bid and takes possession of the deed. The bank transfers the property to its REO (Real Estate Owned) or OREO (Other Real Estate Owned) department, which then prepares the property for sale.

Because preparing properties for sale and selling them costs banks additional money, they're often willing to negotiate sales with investors rather than place the properties on the market.

Admittedly, the process sounds pretty easy, but it can be very challenging for any or all of the following reasons:

- Banks don't like to sell properties at bargain-basement prices just to unload them.
- REO managers often pass the best deals onto their closest contacts and investors with proven track records, so you may need to invest some time in building fruitful relationships.

- REO managers may require you to buy two or more properties as a package deal — you must agree to take one not-so-promising property along with another that has more potential.
- Properties are sold as-is, so you can get stuck with a lemon.

Chapter 12 brings you quickly up to speed with the REO process, reveals ways to contact and work with REO managers, and suggests timing your offer to coincide with the REO department's fiscal calendar.

Finding and buying government properties

The United States government sponsors several programs to encourage home ownership, including HUD (Department of Housing and Urban Development) and VA (Veteran's Administration) financing. Often, borrowers default on these loans, and the government ends up with a property that it doesn't need or want. In addition, state and local governments may seize properties for infrastructure improvements or as a result of unpaid taxes or criminal activities.

As a citizen, you have the right to purchase these government properties, and you can often pick them up at deep discounts. Following is a list of common resources for government-owned properties:

- **HUD and VA repos:** When homeowners default on a HUD or VA home loan, like any lender, the government can choose to foreclose on the property. These are not always the best deals for investors, because HUD and VA homes are commonly listed at or just below market value, but by being persistent, you can often find some pretty good deals.
- **State department of transportation:** The department of transportation commonly buys up property for road improvements and then disposes of the property after completing the project.
- **State or county drug enforcement agency:** If a homeowner is paying for a property with illicit funds or the house is home to criminal activity, the government may step in, take possession of the property, evict the homeowners, and sell the house.
- **County sheriff's office:** When your county sheriff's office seizes a property, perhaps because it was purchased with proceeds from criminal activity, it may offer the property for sale through a broker or at auction.

This list merely introduces the investment opportunities available in government-owned properties. For details on how to find and take advantage of these opportunities, visit Chapter 13.

TIP

A condominium association can also foreclose on a property to collect unpaid condominium fees. Remember, however, that a condo lien is just another lien. The senior lien (first mortgage) takes precedent.

Buying properties from other investors

Some foreclosure investors are more interested in discovering and acquiring foreclosure properties than they are in fixing them up and reselling them. They consider themselves *foreclosure wholesalers* — finding and buying properties and then selling them to other investors.

WARNING!

Generally, I advise against buying properties from foreclosure wholesalers or whatever they call themselves. Whenever someone tries to sell you on some great investment opportunity, ask yourself this question: "If the property were as profitable as this person wants me to think, then why doesn't she fix it up and sell it herself?" Another reason not to buy from other investors, is because by doing so, you're usually paying a markup or finder's fee. Plenty of foreclosure properties are available, and they're not that difficult to track down, so pocket the markup and use that money for renovations or to purchase your next property. Of course, if you've done your research, as explained in Chapter 8, and the price is right, I certainly wouldn't tell you to pass on it.

Just as I advise against buying properties from foreclosure wholesalers, I strongly discourage you from becoming a foreclosure wholesaler yourself. You can make more money by working the foreclosure from start to finish — buy, renovate, and sell. For details about renovating and selling a house for more than you bought it, check out my other *For Dummies* book — *Flipping Houses For Dummies* (Wiley).

Waiting Out the Redemption Period — If Necessary

Many areas of the country give foreclosed-upon homeowners one last chance to get their homes back — through redemption. If the homeowners can come up with enough money to pay off the balance of their loans and all penalties and back taxes, then they get to keep the property. In some cases, homeowners have up to a year to redeem their property before the high bidder at the auction takes possession.

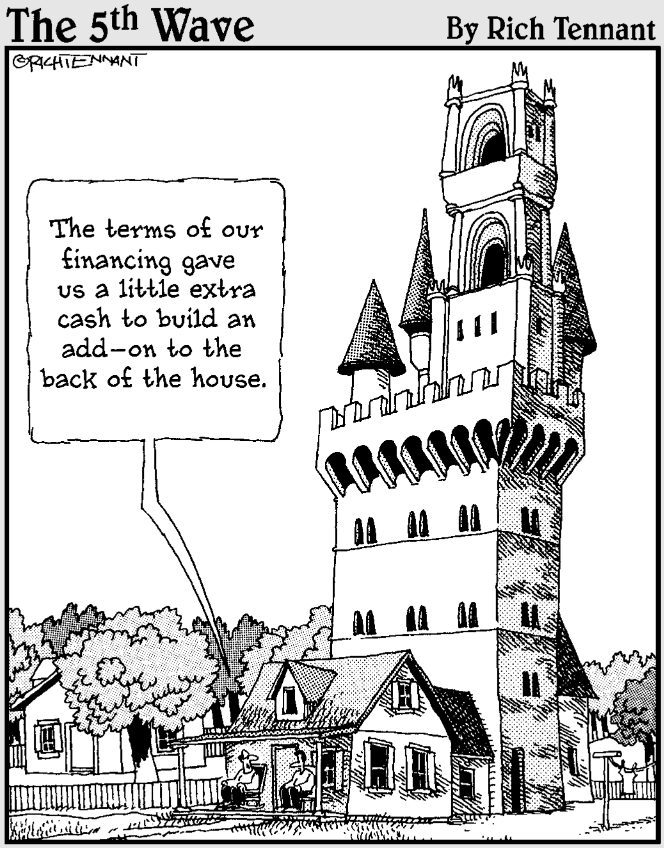
The redemption period can impact you in any of several ways:

- If you purchased the property at auction, you have to wait to do anything to the property until after the redemption period expires. Otherwise, you may invest heavily in renovations only to see the homeowners or another investor redeem the mortgage you bought and cut you out of the deal. You may need to secure the home (particularly if it's vacant) and perform repairs to make the property safe and prevent deterioration, such as from a leaky roof, but invest as little as possible during this period.
- The homeowners may still be able to file for bankruptcy during the redemption period to buy themselves some additional time, which can throw your plans for renovating and selling the property for a loop.
- If another investor purchased a property and is waiting for the redemption period to expire, you still have an opportunity to purchase the property. You can work with the homeowners to bump the other investor out of the deal, redeem the property, and buy it directly from the homeowners.

Surviving the redemption period can be a little tricky, especially if other investors take interest in the property. Chapter 16 shows you what you should be doing during this time to protect your interest. Flip to the appendix at the back of this book to find out whether your state has a redemption period and find out its typical duration.

Part II

Laying the Groundwork for Maximized Profit and Minimized Risk



In this part . . .

Late-night TV real estate gurus lead unsuspecting investors to believe that making tons of money in foreclosures is a snap. That piece of misinformation typically leads the uninformed down a path leading to financial ruin.

By carefully planning and building a road to a successful investment strategy, you can reduce the risk and maximize your opportunity to profit. In the chapters in this part, I show you how to gather the essential information, tools, personnel, and resources to succeed.

Chapter 4

Building a Powerful Foreclosure Investment Team

In This Chapter

- Lawyering up for leads and legal protection
- Tracking down investment capital through a mortgage broker
- Covering your back with a title company and home inspectors
- Contracting out home repairs and renovations
- Weighing the pros and cons of partnerships

At first glance, the investing in foreclosures can seem daunting. You have to know how to find a foreclosure property, finance the purchase and renovations, fix it up, and then sell it . . . all on schedule and typically within a tight budget.

The good news is that you can get by with a moderate amount of knowledge and expertise, as long as you know where and how to find good help. With a list of contacts, a phone, and some people skills, you can delegate your way to successfully investing in foreclosures.

In this chapter, I guide you through the process of building a top-notch team of real estate professionals, consisting of an agent, attorney, mortgage broker, accountant, title company, home inspector, contractors, and additional support personnel.

What role do you play on your investment team? You're the resident foreclosure expert. This book along with the guidance of your real estate attorney, title company, real estate agent, and other real estate professionals can get you up to speed on the process, but when decision time arrives, you're on the hot seat, deciding how much to offer, scheduling the work, and watching the money.

Lawyering Up with a Real Estate Attorney

Real estate deals are primarily legal and financial transactions. Buying foreclosures involves even more legal complexities, so you should never move forward on a deal without competent legal assistance or sign any purchase agreements without the benefit of an attorney's legal eagle eye.

REMEMBER

Don't hire just any old attorney. Look for an attorney with the specialty you need and other qualifications that make the attorney a perfect candidate for the job:

- **Specialty in foreclosures:** Foreclosure laws can be tricky. Choose a real estate attorney who has plenty of experience working the foreclosure circuit.
- **Specialty in bankruptcy:** A real estate attorney who also specializes in bankruptcies is a big plus. In addition to delivering to you expertise on investing in bankruptcy properties, your attorney may steer you to some great leads from his less fortunate clients.
- **Positive personal referrals:** If possible, find a real estate attorney recommended by a friend or relative, instead of simply picking the first attorney you come across in the phone book.
- **Efficient and affordable:** For a lot of foreclosure-action services, look to pay a flat fee, not by the hour or (gasp) minute. For example, an attorney may quote $600 for an eviction action, more if it turns out to be complicated . . . they'll let you know. Look for affordable, not necessarily cheap — you often get what you pay for.
- **Supportive:** Someone who second guesses your decision to invest can paralyze you with doubt. You want an attorney to steer you clear of potential legal pitfalls, but not one who nitpicks every transaction.
- **Available:** A good lawyer is available when you need her.
- **Experienced:** A real estate attorney who owns real estate and rentals or even buys foreclosures is better than one who doesn't.
- **Generous:** A lawyer who shares his leads can help you find properties that you couldn't find on your own. Be careful to avoid sloppy seconds — properties that the attorney sends your way because they're not profitable enough for her.

TIP

If your friends, relatives, real estate agent, title company, or other people you know can't recommend an excellent real estate attorney, call the local bar association for the names and contact information of a few real estate attorneys or bankruptcy lawyers and start from there. In some cases, the attorney you call may not be the right one for you, but he may refer you to someone who is. If all else fails, inquire at a firm mentioned in a foreclosure notice.

Teaming Up with a Good Moneyman — or Woman

Money not only makes the world go 'round, it also moves houses. You need money to purchase a property. Your foreclosure clients may need financing to take action on one of the options you present. And people buying property from you often require financing to close on the deal.

Where do you find all this money? Hunt down someone who specializes in home financing: a *mortgage broker* (commonly called a *loan officer*). By teaming up with a loan officer, you not only have the means to secure financing for your investments, but you also have someone on call for when distressed homeowners need advice or someone interested in purchasing the property from you needs financing.

All mortgage brokers are not necessarily equal, some may not even be licensed, so shop carefully for a quality, licensed mortgage broker. A qualified broker can save you thousands in finance fees and interest. Look for the following qualities in a mortgage broker:

- State licensed.
- Member of the National Association of Mortgage Brokers (NAMB) or the Mortgage Brokers Association (MBA) or both.
- Positive personal referrals from people who have worked directly with the mortgage broker. Ask your attorney, bank, friends, family members, and colleagues for references.
- An understanding of foreclosures, because you need to borrow money based on the future value of the property, not the purchase price. By borrowing on the *future value* (or *repaired value*) of the property, you gain access to more cash for repairs, renovations, and other investment properties.
- No conflicting relationships. A mortgage broker who works in the foreclosure arena my have relationships with homeowners in foreclosure or other investors that may create a conflict of interest.

REMEMBER

Laws require that anyone who wants to loan money work through a licensed mortgage broker, so if you want to use other people's money to finance your investment, you almost always have to work through a mortgage broker or directly with a lending institution, such as a bank.

To obtain assistance from a mortgage broker, consider writing a letter of introduction, like the letter shown in Figure 4-1. Let the broker know that you're going to be investing in foreclosures and you may run into clients who require the broker's assistance.

<Your Name>
<Your Address>
<City>, <State> <Zip>
<Date>

<Mortgage Broker’s Name>
<Company>
<Address>
<City>, <State> <Zip>

Dear Mr./Ms. <Last Name>:

My name is <Your Name>. I am a real estate investor, planning to work with individuals who are going through foreclosure.

I am seeking financing for my investments and will also be exploring various ways to assist distressed homeowners with refinancing into non-conventional mortgages. In many cases, I may need to refer future clients to you for consultation. I believe we can create a win-win situation by working together.

At your earliest possible convenience, I would like to meet with you to discuss financing options for purchasing and renovating investment properties and services you could offer my future clients who may require your assistance.

Please give me a call at <Your Phone Number> or email me at <your email address> if you have any questions or when you have time to meet with me. I look forward to speaking with you soon.

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

Figure 4-1: Sample letter to a mortgage broker.

Consulting a Title Company to Cover Your Back

Although you should hone your own title-inspection skills, a title company offers additional assurance and insurance that the title is accurate and doesn’t have any gaps in its history that could cause problems down the road. Here’s what a good title company can do for you:

- Provide a second set of well-trained eyes to inspect the title and ensure that it's in a recordable form.
- Deliver a *title commitment* and chain of title, showing the history of ownership and any claims against the property. This ensures that the person selling the property is the person who owns it and makes you aware of any liens against or property taxes owed on the property.

REMEMBER

A title commitment is a promise by the title company to insure the title against any future disputes concerning ownership. It typically states who is being insured, the amount of the insurance, a description of the property, conditions that must be met to secure title insurance, and a list of what's not insured.

- Provide title insurance when you purchase the property to protect you from any financial loss if someone has a legitimate claim against the property that the title company missed. The title company also makes sure that any rights to the property, such as mineral rights, are transferred to you (if owned by the seller).
- Highlight any homeowner association liens against the property.
- Inform you of any restrictions on the property or covenants on the land. If you're buying a home in a historical area, for example, the renovations may have restrictions. Certain covenants may prohibit you from removing living trees from the land or limit the total square footage of the house. If these restrictions are valid and you violate them, adjacent property owners can sue you.
- Further educate you concerning foreclosure laws and regulations in your area.
- Provide additional leads on foreclosure opportunities.
- Refer you to other real estate professionals who can assist you with your investments.

Try to hook up with a title company that provides title insurance for the foreclosing attorneys in your area. A company that handles foreclosures regularly knows the common problems to look for in the title. Reputation and location are your two other main considerations. Pick a company that's nearby and has the best reputation for smooth closings. Your real estate attorney or agent can recommend a title company that has a solid reputation in the area. Smaller towns may have only one title company.

TIP

Meet with one of the title company's representatives to explain that you're going to be investing in foreclosure policies. The company may provide you with free title commitments on a few properties in the hopes of gaining your business when you close on a property and need title insurance.

One of the first questions to ask a title company representative is whether the company does title work on foreclosure properties. Many times, underwriters do not do title work on foreclosures. If the company you're considering does not work on foreclosures, keep looking for one that does.

Hiring a Tax-Savvy Accountant

Most of the accounting that applies to investing in foreclosures consists of simple addition and subtraction. Add up the costs of buying, renovating, and selling the house and subtract that from the amount you receive when you sell the house, and if you come up with a positive number, you made money.

Unfortunately, reality is a little more complex, and having a professional accountant on hand can help you avoid unnecessary expenses and legal woes. Your accountant can take all your money and receipts out of your shoe box, sort through them, figure out whether you made any money, and if you did make money, she can calculate the amount of tax you owe. An experienced accountant also delivers the following benefits:

- Saves you money on income tax while remaining in compliance with often complex tax laws
- Ensures that you pay your property taxes on time
- Evaluates your real estate investment activities to determine whether you're considered an investor or a self-employed dealer — essentially the difference between a part-time and full-time investor
- Pays your quarterly estimated taxes if you're considered a self-employed dealer
- Pays your quarterly estimated taxes on your capital gains if you're considered an investor
- May assist you in keeping your renovation expenses within budget

Go with an accountant who has plenty of experiencing keeping the books for real estate investors. If you already have a general accountant who files your state and federal tax returns but has little experience in the real estate arena, consider hiring a different accountant to keep the books for your real estate investments. Ask your real estate attorney or agent for recommendations. Your current accountant may also know someone who's more qualified to deal with real estate. Interview at least three candidates.

If you're good with numbers and have a solid understanding of tax laws that apply to real estate investments, you can take on this job yourself. If you're not real estate tax savvy, however, you can avoid legal headaches and worries by hiring a professional.

Lining Up a Home Inspector

When you buy a property at auction or from a bank, you often agree to purchase it "as is." In these cases, you don't have the benefit of a home inspection before you lay your money down. When you're buying pre-auction properties from distressed homeowners, however, the purchase agreement should state that the transaction is conditional upon the home passing inspection.

By lining up an inspector or team of inspectors ahead of time, you're less likely to pick a sub-standard inspector later in a rush to get the home inspected.

TIP

In the area where I buy most of my investment properties, city inspectors are available to inspect homes prior to purchase. I prefer using city inspectors, because they tend to be more thorough and they're well-versed on local building codes. The city inspectors in our area show up as a team that typically includes a plumber, an electrician, a heating and air-conditioning specialist, a builder, and someone who specializes in zoning. You get a thorough inspection and a complete write-up for about the same price you'd pay a private inspector. However, not all towns and cities offer inspections or they offer them only for new homes.

If you decide to hire an inspector, you can crack open the Yellow Pages and find listings for dozens of home inspectors in just about any area of the country. Finding a qualified home inspector, however, is a challenge. Begin by asking your real estate agent or other real estate professionals you know for references. Another good resource is the NACHI (the National Association of Certified Home Inspectors) Web site at `www.nachi.org`. To track down city inspectors, call your town hall and ask for the building or building code enforcement department. Some counties publish a free county guide that includes all the contact information for city and township offices in the county. You may also be able to access the information on your county's or town's Web site.

When you have a few leads, contact your candidates and ask them the following questions:

- **Are you certified, licensed, and insured?** Certification and licensing ensure that the inspector has the basic qualifications for the job. Insurance may cover any serious defects the inspector overlooks or only the cost of the inspection, depending on state laws.
- **How long have you been a home inspector?** Length of service is often, but not always, a good indication of experience and expertise.

- **How many homes have you inspected?** "One or two," isn't the answer you're looking for. A busy home inspector is usually busy because he's good.
- **What did you do before becoming a home inspector?** Someone who's a retired carpenter or home builder is typically a good candidate.
- **Do you have references I can call?** If the inspector has a good track record, people don't hesitate to provide positive references.
- **Do you recommend repairs or simply identify problems?** Look for an inspector who can recommend repairs and renovations and provide rough estimates for the work.

A homeowner who's selling a property at a clearance price often does so to avoid the costs and headaches of making repairs. Nitpicking can ruin your chances of acquiring a great piece of property. Choose an inspector who focuses more on big-ticket items than on minor defects.

WARNING!

Don't hire your inspector as your contractor — such a move only tempts your inspector/contractor to find more problems with the property.

Contacting Contractors and Subcontractors

When homeowners are facing foreclosure, they don't have a whole lot of money in the cookie jar to maintain their home. In some cases, the homeowners trash the place and even gut the house as a final act of retribution. You usually end up with a property that requires a moderate to major overhaul.

You can do as much of the fixing up as you're qualified, comfortable, and willing to do. For everything else, hire professionals — contractors, subcontractors, or handymen.

- A *contractor* (or general contractor) is the boss. He or she manages the budget and workflow, hires subcontractors, coordinates the work from start to finish, and hands you the bill.
- *Subcontractors* perform specific tasks, such as wiring, plumbing, installing ductwork, replacing roofs, laying carpet and so on.
- *Handymen* are skilled, jack-of-all-trade laborers who handle general repairs, landscaping, and minor renovations.

In the following sections, I explain the duties of a general contractor and methods for finding and hiring contractors, subcontractors, and handymen.

Hiring a general contractor — or not

On isolated jobs — jobs that require only one or two subcontractors — you can often do the contracting yourself, just as if you were having your washer or dryer repaired. For more extensive projects that require the coordination of multiple subcontractors, a general contractor may be better suited.

TIP

To me, a general contractor represents additional overhead I shouldn't need to pay for. By working closely with the subcontractors to coordinate the work, you should be able to handle the general contracting yourself, but if you have any doubts about your own abilities in managing the project, hire a qualified contractor. You should also consider using general contractors if you're working on more than a couple projects. You have enough to do just managing your portfolio.

If you choose to do the general contracting yourself, you assume the following responsibilities:

- Budgeting
- Hiring
- Scheduling
- Supervising
- Firing
- Negotiating costs

WARNING!

When acting as contractor, obtain a permit before starting work on any project that requires a permit, such as a room addition, a deck, a garage, or even a fence. If you don't obtain a required permit and something bad happens, you may ultimately be responsible, even after you sell the property. You can usually pick up an application for a building permit at the office of the municipality in which the property is located. Call town hall and find out the office you need to visit, or consult your handy-dandy county guidebook (if you have one).

If you decide to hire a general contractor to manage a big project, such as a room addition, kitchen or bathroom overhaul, or adding a second story onto a house, provide a detailed description of the work you want done and let the contractor know that you're going to hold him to his estimate. Some contractors are notorious for presenting low estimates and then performing additional work to jack up the cost. Contractors want repeat business, so let them know that if you have any problems, you won't be calling them back. Have this conversation before the work begins and before you award the contract to them, so you can remind them of that conversation if any issues crop up.

Tracking down top-notch contractors and subcontractors

Ask other homeowners and real estate professionals to recommend the contractors and subcontractors they've used. A good place to start is with your real estate agent. Agents typically have a computer packed with references for affordable, honest contractors who do high-quality work because agents often need to call in a contractor to whip a home into shape before placing it on the market. Your local hardware store may also be a good source for recommendations. Don't rely on ads in your local newspaper, on the grocery store bulletin board, or in the phone book.

WARNING!

To lessen the risks of getting ripped off, do your due diligence: Check references, workmanship, the amount of time the contractor has been in business; ask the contractor if he's licensed and insured; and check with the state or your local Better Business Bureau to see if anyone has filed a recent complaint against the contractor.

Contracting with contractors and subcontractors

When you're hiring a contractor or subcontractor, you have three goals. You want the job completed to your satisfaction, on budget, and on schedule.

When you get the contractor's estimate and proposal, attach a one-page agreement to it that includes the following:

- Start and end date.
- A $50 penalty for every day that the project runs over schedule. If the contractor's proposal indicates that the work can be completed in 30 days, you may add a clause that states that if the work is not completed in 45 days, $50 per day will be deducted from the final cost.
- A condition that the contractor must notify you before performing any additional work that's not stipulated in the original proposal. Contractors who have been in business for awhile know pretty darn close to how much a job is going to cost. By steering clear of any changes or upgrades, you should be able to remain within budget.

Your job's not over after you sign the agreement. Remain vigilant to keep the project on schedule and within budget:

- Let your contractors know when the For Sale sign is going up.
- Give them what they need to succeed, including deposits and supplies.
- Have them furnish you with receipts of their purchases.
- Show up unannounced at the worksite to see whether they're working.
- If the workers are doing a good job, tell them so, and do it often.
- Don't strive for perfection, but don't overlook shoddy work just to keep the peace either. You're paying for a job done well, not just a job done.

Whenever you have to rely on someone else to do work for you, you take some risk. To limit your exposure to risk with contractors, take the following precautions:

- When hiring a contractor or subcontractor, make sure that the person is insured against both property damage and personal injury. An average hospital bill can wipe out your profit.
- Be careful about deposits, especially when you're dealing with a contractor you don't know. Contractors have been known to take the deposit and disappear. A 25–50 percent deposit is normal — generally, the smaller the contractor the larger the deposit. You can pay most handymen on a week-to-week basis.
- Be careful handing huge chunks of money to a contractor. If the contractor needs a costly supply of materials to get started, consider paying the supplier directly.

Pay your contractors as soon as they complete their work to your satisfaction. My father was a builder, and my brother Jeff, who's now my property manager, worked very closely with him. Jeff has a pay-as-they-go policy — pay your contractors as they're pulling out of the driveway. This is one of the best ways to show your appreciation for a job well done.

My contractor went AWOL!

You can reduce your risks of losing money to a contractor, but you can't eliminate those risks. I had a great contractor for a long time. After hiring him to rehab dozens of houses, I gave him a $3,500 dollar deposit on a Thursday, for a roofing job he promised to complete by the following Tuesday.

The contractor failed to mention that he had planned a weekend trip to Las Vegas. When he returned, the deposit was gone — gambled away in Lost Vegas. What happens in Vegas stays in Vegas must be true, because my money stayed in Vegas, along with the reputation of my contractor. I lost a good contractor, and he lost a good account. He wanted to do business with me again but I just couldn't allow it.

Finding a handyman and other helpers

You don't necessarily need a licensed subcontractor to do odd jobs around the house. A handyman (someone who's handy with power tools and hand tools) can often complete small jobs for a fraction of the cost. If the house needs all new wiring or plumbing or has structural damage, pay a little extra for a licensed expert. For smaller jobs, such as leaky faucets, clogged drains, replacement windows, and new doors, a good handyman is a more affordable choice.

Insuring your helping hands

Your contractor should supply you with a separate *proof of insurance* form, attached to the bid that verifies that the contractor and his workers are insured for this particular job. If you're hiring a subcontractor or handyman who's moonlighting from his day job, he may be covered under his company's insurance policy, but he may *not* be covered during his stint as a moonlighter.

WARNING!

When hiring a contractor or handyman who can't provide you with proof of insurance, contact your insurance company and take out a separate workman's comp policy (or add coverage to your current policy on the house you're renovating) that covers anyone who's working on your house. Added insurance takes a little extra time and costs a few hundred dollars, but if you're not covered and a worker is injured on the job, he may sue you and you may lose your entire profit and even some of your own personal savings.

Selling Your Property for Top Dollar through a Seller's Agent

If you plan on selling the properties you buy, a top seller's agent can assist you in marketing the property and selling it quickly and for top dollar. I strongly encourage you to enlist the aid of an agent in selling your investment properties. What you pay in commissions, you usually earn back with interest, because a great agent can sell the property for more money in significantly less time than you can on your own.

In the following sections, I explain the beneficial services that agents can provide and offer guidance on finding the best agent for your flipping needs.

Seller's agent versus buyer's agent

Real estate agents often excel in one area — buying or selling homes. Buyer's agents are better at finding the right homes at the right price for home buyers. Seller's agents are more skilled at selling homes quickly for top dollar. A good agent may also have access to information that can help you find and evaluate properties in the foreclosure process. Some agents may even specialize in working with investors. Others may be experts in property management and relocations and can help buy-and-hold investors find tenants for their rental units.

When buying foreclosure properties at an auction, you don't need an agent to assist you in finding the right home for your needs. You need an agent who can sell the property quickly for a price that's in line or slightly higher than the going price in your market.

When you're head hunting for an agent to work with, ask her what she excels in and then ask around to make sure you're getting one of the top seller's agents in your area.

Recognizing the value of a seller's agent

A seller's agent who has plenty of experience working with investors, can assist you with more than selling the property. A top-selling agent also helps you:

- Evaluate the value-add and cost-effectiveness of renovations.
- Locate contractors, subcontractors, and other professionals who have a good track record.
- Stage your house (make it look pretty) for showings. A properly staged home, on average, sells in half the time for 7–10 percent more than an un-staged home.
- Market your rehabbed home to every real estate agent in the neighborhood via the Multiple Listing Service (a listing of homes for sale that goes out to all the real estate agents in your area).
- Evaluate offers on the rehabbed home and guide you in picking the best of the bunch.
- Navigate the closing to ensure smooth sailing.
- Advise you on how much rent you can charge for a property if you want to hold onto it for awhile and you need some cash flow.

WARNING!

On average, you take twice as long selling a property yourself than you do when you work with a real estate agent, and every day your home sits on the market costs you money.

Real estate agent or Realtor: What's the difference?

A real estate agent is anyone who has a state license to negotiate the sale or purchase of a property and works for a real estate broker or brokerage company. A Realtor is a real estate agent who's also a member of The National Association of Realtors. The U.S. has more than 2 million real estate agents, but only 1.2 million are Realtors.

Because the qualifications for obtaining a real estate license vary from state to state, the quality of real estate agents varies much more than the quality of Realtors. The National Association of Realtors requires its members to complete additional training and testing to improve their knowledge and abilities and encourages members to follow a strict code of ethics. The association also provides its members with additional resources and tools to assist in finding and marketing properties effectively. Being a Realtor costs more, so when you hire Realtors, you know you're getting people who've made an investment in themselves.

Of course this association membership doesn't mean that a particular Realtor is more qualified than a given real estate agent, but the odds are pretty good that you receive superior advice and service from a Realtor. To find a bona fide Realtor, look for the Realtor logo on business cards and stationery. Almost all Realtors make a point of proudly displaying this logo. You also can find a Realtor in your area by checking out `www.realtor.com`.

Picking an agent with the right stuff

Any licensed real estate agent can sell your house for you, but you want someone whose experience and training are rooted in sales. A top agent typically has the following credentials:

- Five or more years experience
- GRI (Graduate Realtor Institute) certification
- CRS (Certified Residential Specialist) certification
- Realtor status (not simply a real estate agent)
- A consistent top-5-percent performance in the marketplace
- Assisted by a clerical staff
- Well-connected with other agents
- Works for a real estate company that has a Web site
- Maintains a personal Web site or a blog
- Closely involved with the community (the more the agent's involved, the more committed she is to doing a good job)

For assistance in finding a qualified real estate agent who can work with you to track down pre-foreclosure or foreclosure properties, visit `www.HurryHome.com`. You can sign up for access to insider information and unlisted properties, and the service can put you in touch with a qualified real estate agent who specializes in the types of properties that fit your investment strategy. Also check out `www.GuthyRenkerHome.com`, where you can also find some excellent articles on real estate topics.

Another way to find an agent is through referrals from other homeowners (buyers and sellers), other investors, or your real estate attorney or title company. When you have a list of 10 to 15 names, start calling around and interviewing candidates to compare their experience, education, and certification as described in the preceding list.

The size of the real estate company doesn't matter. Whether the agent is with a large franchise, a regional company, or an independent office makes no difference. Interview several agents. If their qualifications seem about equal, pick the person that you're most comfortable working with.

Many books on real estate investing recommend that you try to convince the agent to accept a lower percentage in commissions or a flat fee for helping you buy or sell a property, but this can backfire. I suggest that you find the best agent and then pay the agent the going rate or a little more. When you pay less, your agent is going to work harder for the clients that are paying more, and no card carrying capitalist can blame them.

Assessing the Pros and Cons of Partnerships

Taking on a partner is like getting married, so if you don't trust a person as much as you trust your spouse, you probably shouldn't become partners. Great partnerships are rare, but when they work they enable both parties to achieve more than they could achieve individually. All too often, however, a partner runs off with the cash, fails to pay the contractors, cashes checks made out to the water company or building supply store and pockets the money, files an insurance claim to collect for damages without your knowledge, or figures out some other way to pick your pocket.

If you're considering partnering up with someone, think about having the person work for you for a fee. That removes one possible area of conflict, and if the relationship doesn't work out, you're only out the money you paid the person up to this point.

Thriving partnerships always require constant attention and nurturing. To establish a productive partnership, take these seven steps:

1. **Pick energetic, talent, and determined partners whose personalities and talents complement yours.**
2. **Address financial concerns up front.** Don't partner with someone who has little or no income, a poor credit rating, lousy cash flow, or is in a precarious financial position. Each of you should fully disclose up front your financial situation and how the money is to be handled.
3. **Build a common vision with shared goals.** You both need to be on the same page.
4. **Communicate, communicate, communicate.** Communications should be frequent, open, and honest.
5. **Promise only what you can deliver, and then deliver on those promises.** This builds trust.
6. **Share decisions, work, and rewards equally.**
7. **Be prepared to compromise.** "My way or the highway" doesn't always work. Try on your partner's ideas and approach every once in awhile to see how it works.

If you partner with someone, have your attorney write up a contract that details the responsibilities of each party and how profits are to be divided. A partnership that's based only on a handshake often ends up in a bitter battle.

Chapter 5

Filling Your Foreclosure Tank with Financial Fuel

In This Chapter

- Calculating the amount of cash you need
- Sampling your financing options
- Using your investment property as collateral
- Exploring conventional loans
- Comparing the cost of two or more loans

When the average homeowners purchase a home, they typically finance their purchase with a conventional loan, but in the land of foreclosure investing, cash is king. Cash gives you a competitive edge over other investors who have to wait around for loan approvals, appraisals, and other delays that can quickly sink a deal. With cash in hand, you can offer distressed homeowners immediate solutions, scoop up properties at auctions, and get the best deals on REO properties.

In this chapter, I show you how to estimate how much cash you need and assess a variety of conventional and creative financing options.

REMEMBER

When I say that you need cash to invest in foreclosures, I don't mean that all the cash must be your own. You can borrow the money, but you need to borrow it in a way that makes the cash readily accessible. Ready cash enables you to wrap up a transaction quickly.

Estimating Your Cash Needs

The standard way of buying a house is to figure out how much house you can afford, get pre-qualified for a loan, and then start shopping for homes in your price range. You don't need cash. You simply need enough income coming in every month to cover the loan payments.

When buying foreclosure properties, the process is reversed by the need for cash. First, you gather the cash you need, and then you go shopping. So the first step is to figure out how much cash you really need.

Pick a price range that's comfortable for you. Are you planning on buying homes in the $50,000, $100,000, $200,000, $500,000, or $1,000,000 range? Choosing a price range in a particular neighborhood benefits you in two ways. It enables you to more accurately estimate your cash needs and evaluate the worth of comparable properties in that price range.

WARNING!

When picking a price range, stay in your comfort zone. Sure, you stand to earn a higher profit with pricier properties (a 20 percent profit on a million dollar home is $200,000, whereas it's only $20,000 on a $100,000 home), but a 10 percent loss on a million dollar home is $100,000, whereas it's only $10,000 on a $100,000 home. In addition, repairs, holding costs, and other expenses are exponentially higher for million dollar homes. When you're first starting out, make your expensive mistakes with smaller amounts of money.

To calculate a ballpark figure for the amount of cash you need to buy, hold, and renovate a property, account for the following costs:

- Purchase price of the property.
- Loan costs — upfront costs for securing a loan, such as loan origination fees or points.
- Monthly holding costs (loan payments, insurance, property taxes, utilities) multiplied by the number of months you plan on owning the house. You're better off calculating your holding costs, but holding costs generally run about 10 percent of the purchase price for the duration of the project.
- Repair and renovation expenses typically hover around 10 percent of the purchase price.
- Add another 10 percent or so for marketing and selling the property.
- Miscellaneous costs, including title insurance and closing costs at time of purchase.

Here's a miniform you can use to calculate a rough estimate of the amount of cash you need:

Purchase price:	$__________
Loan costs:	$__________
Holding costs:	$__________
Renovation expenses:	$__________
Selling expenses:	$__________
Miscellaneous expenses:	$__________
Total:	$__________

After you determine a rough estimate of the amount of money required to buy, hold, and sell a foreclosure property, you're ready to evaluate your financing options and then start shaking the bushes for the financing you need to fuel your investment.

Finding a Cash Stash: Knowing Your Financing Options

People often talk themselves out of buying a house or investing in real estate, falsely believing that they "can't afford it." The truth is that money is readily available. You just need to know where to look for it, and the first place to look is a mortgage broker. In Chapter 4, I show you how to find a qualified mortgage broker (or loan officer).

A mortgage broker can quickly assess your situation and your investment plans and reveal your financing options. These options include the following:

- **Hard-money loans:** High-interest, short-term loans that are often attractive to investors who can't qualify for conventional loans. For more about hard-money loans, check out "Borrowing Against the House You're Buying," later in this chapter.
- **Your own money:** Cash and savings, equity you've built up in your home (your home's value minus what you owe on it), and retirement savings. See "Shaking Your Piggybank: Tapping Your Own Resources," later in this chapter, for details.
- **Personal loans:** Cash from family members or friends who are either willing to help you or wanting to invest money without having to do all the work.

- **Conventional loans:** Money you qualify to borrow from a bank or other conventional lending institutions based on your income, net worth (the value of what you own minus the value of what you owe), and credit history. To find out more about conventional loans, check out "Financing Your Venture with Conventional Loans," later in this chapter.
- **Government loans:** If you're buying properties from government-sponsored programs, you may qualify for government loans, even as an investor. See Chapter 13 for details.
- **Credit card loans:** Some investors shore up their investments or pay for renovations using their credit cards. If you can flip the house quickly and pay off your credit card charges within a few months, this option isn't as risky as you may think. I discuss the credit card option later in this chapter in the section "Maxing out your credit cards."

TIP

Whenever you're using your own money to finance real estate investments, you place your personal savings and your home at risk. As much as possible, choose financing options that expose you to less risks:

- **Least risky:** Borrowing money against the foreclosure property you're buying. If the deal goes belly-up, you stand to lose only that property, not your own home. See the next section, "Borrowing against the house you're buying."
- **Moderately risky:** Refinancing your home or taking out a home equity loan. By cashing out the equity in your home, you lose one of the best buffers you have to get you through hard times if you encounter financial hardship. See "Unlocking the equity in your home," later in this chapter.
- **Real risky:** Burying yourself in credit card debt is risky, but it's often a viable option if you don't have the cash on hand to pay for repairs and renovations. Instead of letting the house just sit there, get the repairs and renovations completed, even if you have to use your credit card to pay for them, and then place the house back on the market, sell it, and pay off your credit card charges. See "Maxing out your credit cards," later in this chapter for details.

In the following sections in this chapter, I describe these options in greater detail, provide tips on how to make yourself a more attractive borrower (so you can borrow more money at lower interest rates), and compare the costs of various loans.

TIP

Whey you buy a home to reside in with your spouse, I recommend that you own the home jointly, but when buying investment properties, only one of you should sign the mortgage and promissory note (the promise to pay), if possible. This puts the property you own jointly at less risk. In some states, any real estate owned by the husband is also owned by the wife, but not vice versa, so this may not be an option for men . . . sorry fellas. Consult your attorney and accountant to determine strategies for lowering your exposure to risk.

Leveraging the power of Other People's Money (OPM)

One of the secrets to maximizing your investment profits is to use as little of your own money and as much of other people's money as possible. The magic of using other people's money is in the numbers, as the following examples reveal:

- You invest $100,000 to buy, renovate, and sell a house for $120,000. You just made a 20 percent profit ($20,000 profit divided by your investment of $100,000 equals 20 percent).
- You invest $20,000, borrowing the other $80,000 to buy, renovate, and sell a house for $120,000. You just made a 100 percent profit ($20,000 profit divided by your investment of $20,000 equals 100 percent).

In these examples, although you earn the same profit in terms of dollar amount, when you look at percentages, you earn five times more profit by using other people's money. You may argue that you still end up with $20,000 in your pocket either way. But say you have $100,000 to invest, as in the first example. Instead of buying one property using $100,000, you could divvy it up into $20,000 chunks to buy five $100,000 properties (borrowing $80,000 for each). When you sold the properties, you'd earn $20,000 each for a total profit of $100,000!

Borrowing money is always risky, but you have to take some risk. Throughout this book, I show you ways to reduce the risk, but unforeseen events can undermine the best-laid plans. As a real estate investor, you need to decide for yourself if the potential benefits outweigh the risks.

Borrowing Against the House You're Buying

Lenders always require some *collateral* to secure the loan — something of value they can take from you and sell if you happen to default on the loan. You can use your own house, possessions, and retirement savings as collateral, but that places your current possessions at risk. A safer way to borrow money is through a *hard-money lender* who's willing to accept the investment property as collateral. You can often locate hard-money lenders through your mortgage broker.

Hard money is a high-interest, short-term loan that offers three big benefits:

- You get access to cash you may not be able to get through a conventional lender.
- Hard-money lenders often accept the future value of a property as collateral, so you don't have to borrow against your own home.
- You can often set up a separate escrow account with a hard-money lender to pay for repairs and renovations.

Now for the bad news. Hard money is called "hard" for several reasons. Before choosing the hard-money option, be aware of the following key areas of hard-money loans.

- **Points or discount points:** You can expect to pay anywhere from 2–6 points for the loan up front. A point is 1 percent of the loan amount, so if you're paying 6 points on a $200,000 loan, you're paying $12,000 up front to get your hands on the money.
- **Interest rates:** Hard-money lenders often charge nearly double the interest rates of conventional loans. If the going interest rate for conventional loans is 6.5 percent, for example, a hard-money lender may charge 10–15 percent.
- **Loan-to-value (LTV):** Hard-money lenders typically approve you for a loan of only 50—70 percent of the expected sales price of the property, so you need to be sure that you're buying the property for 30 percent or more below what you expect to sell it for, and you may need additional funds to cover holding and renovation costs. When buying into a declining market, LTV becomes even more critical, because your loan amount stays the same while housing values are declining. If the value of the house dips below what you owe on it, you place yourself in a situation of owing more on a property than what you can sell it for.
- **Amortization:** Hard-money lenders often want to amortize the loan over 5–15 years instead of the standard 30 years, which ends up increasing your monthly payments, because you're paying down the principle on the loan faster.

  TIP

  To lower the monthly payments, amortize over 30 years or negotiate for interest-only payments. You want to have enough free-flowing cash to finance renovations and cover your holding costs.
- **Balloon payment:** Hard money typically has balloon payments or *cash calls* after so many months, or you may be required to pay off the loan in full in a matter of 6—36 months. This isn't a problem as long as you have a solid plan in place and sufficient funds on hand for when the balloon payment is due.
- **Prepayment penalties:** Avoid any loans that stipulate a prepayment penalty — extra money you have to pay if you choose to pay off the loan early. I've seen investors lose thousands of dollars when they sold a house because they agreed to pay a 2–3 percent prepayment penalty.
- **Closing costs:** As with any lender, you have to close on a loan from a hard-money lender. Figure in the cost of the title insurance, closing fee, credit report, and appraisal survey. Be particularly careful of any discount points or loan origination fees — these are areas where the lender and mortgage broker can really jack up the cost of the loan.

Putting the cost of hard money in perspective

Hard-money loans may be the most costly, but don't worry so much about what the hard-money lender is charging and how much profit he's earning. Calculate the cost of the loan into your investment, just as you calculate in repair and renovation costs.

If you calculate in all your costs and can still make a 20 percent or higher return, who cares what the other guy is making? See "Comparison Shopping for Low-Cost Loans," near the end of this chapter for instructions on how to calculate the total cost of a loan over the life of the loan.

- **Cross-collateralization:** If you're investing in two or more properties, the hard-money lender may want to *cross-collateralize* the properties. If you sell one property for a $10,000 profit, for example, the lender may want to use the profit to pay down the loan on the other property. This isn't terrible and may even benefit you by reducing your interest on the second loan, but it's something you should be aware of. Cross-collateralization simply secures the lender's position.

Some hard-money lenders offer something called a *bullet loan*, in which you make no monthly payments. Interest accrues and is rolled back into the loan's principal, which increases the total amount required to pay off the loan and can significantly increase the total amount of interest you end up paying. However, a bullet loan frees up your cash flow, so you have more money on hand for renovations and other investment properties.

WARNING!

Don't borrow money from a hard-money lender and give her a deed in advance in case you do not perform. This takes away some of your rights. Hard-money lenders are normally not licensed to provide loans. They purchase loans through others. If you default on the loan, they won't send Guido to break your legs. They just repossess the rehabbed property you put up as collateral.

Shaking Your Piggybank: Tapping Your Own Resources

You may be one of the few fortunate investors who has enough cash in your piggybank to fuel your investments. The total cash in your piggybank may be a little difficult to see and to calculate at first. If the cash is readily available — just sitting in your bank account — that's easy, but you may have less readily available cash locked up in your house, other investments, or retirement accounts.

In the following sections, I explore the pros and cons of using your own money to finance your investments, and then I assist you in identifying sources of cash that may be locked up in other assets.

When you first start investing in foreclosures, keep your day job. A steady income enables you to qualify for loans and keeps you afloat in the event that your investments prove to be less profitable than expected.

Examining the pros and cons of using your own money

If you're single or you and your significant other are on the same page about this foreclosure investing thing, cracking into your nest egg to finance your investments may be the quickest way to get your fingers on some investment capital. Be aware, however, of the potential benefits and drawbacks of using your own money:

- Tapping your cash reserves places you at greater financial risk, because if anything goes wrong — you get laid off or fired, become too ill to work, or encounter unexpected expenses — you may have less reserves to keep you afloat. Using your own money, however, also reduces your risk, because you're not signing some promissory note agreeing to pay back a loan by a specific date.
- Limiting your investment capital to the amount of cash you have on hand saps your purchasing power — you have to buy houses in a lower price range and may not have sufficient cash to properly renovate the property.

A great way to ruin a relationship is to bet the farm on big profits without the knowledge and complete agreement of your spouse or significant other. If your investment doesn't pan out, and even if it does, your spouse may take offense at not being consulted.

Totaling your sources of investment capital

You may have more money than you realize, especially if you own your own home and have done a good job of managing debt. In the following sections, I reveal several sources of personal investment capital that may provide you with a solid chunk of the cash you need.

Counting your money in savings

The most obvious source of cash is sitting in your bank accounts — savings and checking. Tally up your personal savings and see how much money you have on hand.

WARNING!

Wiping out your savings and checking accounts is never a good idea. If you don't have enough in savings to cover the next three months' worth of bills, seek investment capital elsewhere. Keep a sufficient cash reserve on hand just in case you experience a financial setback.

Unlocking the equity in your home

Your home is not only a place to live. It may also be a cash cow, especially if you've been paying down the mortgage principle for several years and the value of your home has appreciated significantly during the time you've owned it. You can unlock the *equity* in your home. Equity is a measure of your home's currently appraised value minus the amount you owe on the home. If your home appraises for $200,000, for example, and you owe $125,000 on it, you have $75,000 in equity.

You can unlock the equity in your home in one or both of the following ways:

- **Refinance the mortgage:** Take out a new mortgage on the home for the amount of its currently appraised value and pay off the old mortgage. (You can refinance for less than the appraised value to cash out only a portion of your equity.)
- **Take out a home equity loan or line of credit:** A home equity loan, separate from the mortgage, enables you to take out a loan up to the amount of equity in the home. With a home equity line of credit, you have an account from which you can draw money at any time. You pay interest on only the money you draw from that account.

See "Financing Your Venture with Conventional Loans," later in this chapter for tips on finding the lowest-cost loans available.

Maxing out your credit cards

Maxing out your credit cards to purchase a car, clothes, electronics, groceries, and other items that provide no return on your "investment" is never a good idea. Using your credit cards to purchase investment properties that offer a solid, relatively quick return on your investment, however, can be a savvy financial move. Following are some tips to maximize the use of credit card debt when investing in real estate:

- **Shop for credit cards with the lowest interest rates.** Don't look at the low introductory rates; read the fine print to find the rate after the introductory period expires.
- **Check your credit card statements to determine your current limits.** Depending on your credit history and the credit card company, you may have a credit limit in excess of $10,000 per card.
- **Pay off your charges as quickly as possible.** Paying off your credit card debt quickly not only saves you from paying high finance charges, but it can also raise your credit rating, so you qualify for future loans at lower interest rates.

Real estate investors rarely use credit card debt to finance a purchase. They use it more often to finance repairs and renovations, so they can quickly resell the property and pay off their credit card charges in full.

REMEMBER

If you can purchase and sell the property quickly and pay off your charges in a month or two, credit card interest is unlikely to consume a big chunk of your profit. Years ago, when I first started, when the bank of Grandma was running low, I would buy houses with credit cards. I even attended a seminar that recommended accumulating lots of credit cards. I would never suggest this strategy today. Use a credit card only for emergencies.

Tapping into your retirement savings

More and more investors are choosing to set up *self-directed* IRAs and other types of retirement accounts that enable them to invest in real estate rather than in stocks and bonds. The reasoning behind this is that real estate often provides a better and sometimes even more secure return on your investment.

With a self-directed IRA, you can buy and sell properties out of your retirement account. Setting up a self-directed IRA, however, is no simple matter. Typically, a trust company manages the money and properties in the account, and all profits and losses from your investments must stay in that account. Withdrawing money from the account results in the same IRS penalties you have to pay if you withdraw money from any type of retirement account.

TIP

Consult your financial advisor and accountant for details about using a self-directed IRA to finance your foreclosure investments. If a self-directed IRA is not a viable option, you may be able to borrow money against your retirement account. Keep in mind, however, that borrowing against your retirement savings places that savings at risk, as does any other investment.

Planning for contingencies

For every plan you have to buy a foreclosure property, have a plan B. Your plan B should cover contingencies in the event that the deal doesn't quite proceed according to plan A. Your contingency plan should cover the following unexpected events:

- **Delays:** Homeowners can work out a deal with the lender at the last minute or file for bankruptcy. Courts can add further delays. If your area has a mandatory redemption period, this can be a huge delay. You may also have trouble selling the property after you fix it up — do you have enough money to hold onto the property if it lingers on the market?
- **Mistakes:** What if you pay too much for a property? What if the market dips right after you buy the property, so you can't sell it at a profit? Plan on making a few costly mistakes, especially when first starting out.
- **Cost overruns:** Rarely do renovations cost *less* than you expect. Undetected defects in the property can increase repair bills. Irate homeowners can trash the property and steal the kitchen sink and cabinets on their way out the door. Contractors may overcharge you. Do you have enough money to cover unexpected expenses?

TIP

To protect yourself against unexpected expenses and scheduling delays, take the following precautions:

- Buy properties for at least 25 percent less than you know you can sell them for. If you make a mistake, a 25 percent buffer can usually bail you out.
- Don't get in over your head. Assume that your total investment is going to be at least 20 percent more than you anticipate, and have access to enough cash to cover that additional 20 percent.

WARNING!

Hope for the best, but plan for the worst. Without an effective contingency plan in place and a sufficient financial buffer, you may end up in foreclosure.

Financing Your Venture with Conventional Loans

To get a conventional loan, you hand your bank or mortgage broker your financial records, including pay stubs, tax returns, bank statements, and documents showing how much you own and owe, and your bank or mortgage broker does a little extra research to determine how much you qualify to borrow.

In the following sections, I show you how to make yourself an attractive borrower, so you can borrow more money at lower interest rates, and how to gather the paperwork you need to apply for a loan.

WARNING!

Although I'm a big proponent of financing investments with other people's money, always treat that money as if it were your own money, and don't get addicted to it. I've seen business owners use other people's money to finance drug habits, personal purchases, and other indulgences, and it always turns out bad. Show respect for the right to borrow other people's money by choosing smart investments and paying back those loans on time.

Making yourself look good on paper

Real estate investors with proven track records have no problems finding lenders eager to loan them money. Until you achieve platinum status, however, you'd better look good on paper. You need to demonstrate that you have a solid income from your day job, money in the bank, investments, or assets that you can sell. You need proof that you pay your bills on time. And you need to show that you're not so heavily burdened by debt that one more loan is likely to push you into bankruptcy.

The following sections take a snapshot of your financial picture and highlight the details that lenders commonly consider before approving a loan. By identifying areas of improvement, you can hammer out the dents to make yourself look as good as possible to prospective lenders.

Determining what you're worth in dollars and cents

The first question a lender is going to ask you is "What's your net worth?" Net worth is simply whatever money you would have if you sold all your stuff and then paid off all your debts, including your taxes. Officially, the equation goes like this:

Net Worth = What You Own–What You Owe

To prove to a lender that you're a worthy borrower, type up a page that lists your assets and liabilities and calculates your net worth. Don't forget about your personal and household belongings, art collection, model train collection, jewelry, antiques, and so on. Hopefully, the result is a positive number.

TIP

A strong net worth can help you borrow money at competitive interest rates, but you can still borrow money with a low or even a negative net worth. If you have a solid investment strategy and the energy and commitment to implement it, you can secure the capital you need to get started. You simply may have to settle for a hard-money loan, as explained earlier in the section, "Borrowing Against the House You're Buying."

Obtaining your credit report

Your bank or mortgage broker is going to inspect your credit history before approving a loan, so you should know ahead of time what that credit history says about you. Check your credit report every three months or so, correct any errors, and take steps to improve your credit rating. No irregularity is too small to correct.

You can obtain your credit report through any of the following three credit reporting services, but because lenders may report to only one service, ideally, you should check all three:

- **Equifax:** (800) 685-1111 or online at `www.equifax.com`.
- **Experian:** (888) 397-3742 or online at `www.experian.com`.
- **TransUnion:** (800) 916-8800 or online at `www.transunion.com`.

For the complete picture of your credit history, request a tri-merge report that compiles information from all three credit reporting agencies. Some creditors don't report to all three agencies, but when lenders check your credit history, they're probably going to look at everything, so you should, too.

Read on for details about obtaining, inspecting, and correcting your credit report.

TIP

As of September 1, 2005, the Federal Trade Commission has made it mandatory for the three major credit-reporting companies to provide you with a free credit report once every 12 months. To obtain your free credit report, do one of the following:

- Submit your request online at `www.annualcreditreport.com`.
- Phone in your request by calling toll-free 877-322-8228.
- Download the Annual Credit Report Request Form from `www.annualcreditreport.com/cra/requestformfinal.pdf`, fill it out, and mail it to Annual Credit Report Request Service, P.O. Box 105281, Atlanta, GA 30348-5281.

Examining your credit report

When you receive your credit report, inspect it carefully for the following red flags:

- Addresses of places you've never lived.
- Aliases you've never used, which may indicate that someone else is using your social security number or the credit-reporting agency has mixed someone else's data into yours.

- Multiple social security numbers, flagging the possibility that information for someone with the same name has made it into your credit report.
- Wrong date of birth (DOB).
- Credit cards you don't have.
- Loans you haven't taken out.
- Records of unpaid bills that you either know you paid or have good reason for not paying.
- Records of delinquent payments that weren't delinquent or you have a good excuse for not paying on time.
- Inquiries from companies with whom you've never done business. (When you apply for a loan, the lender typically runs an *inquiry* on your credit report, and that shows up on the report.)

WARNING!

An address of a place you've never lived or records of accounts, loans, and credit cards you never had may be a sign that somebody has stolen your identity. Contact the credit-reporting company immediately and request that a fraud alert be placed on your credit report. For tips on protecting yourself against identity theft and recovering from it, check out *Preventing Identity Theft For Dummies* by Michael J. Arata, Jr. (Wiley).

Boosting your credit score

Last but certainly not least: Your credit report should contain your credit score. (If it doesn't, contact the credit-reporting agency and request your score.) Credit-reporting agencies often assign you a credit score that ranges roughly between 300 (you never paid a bill in your life) and 900 (you've had a credit card for a long time, borrow small amounts often, always pay your bills on time, and don't carry any huge balances). Each credit reporting agency may use a different scoring method and range of scores, so you can expect some variation.

Your credit score determines not only whether you qualify for a loan but also how much you're qualified to borrow and at what interest rate. A high credit score lets you borrow more money at a lower interest rate.

TIP

A credit score of 700 or higher is superb. Anything below about 680 raises red flags. If your credit rating dips below 700, take steps to improve it, such as the following:

- Dispute any erroneous items on your credit report. Most credit-reporting agencies supply you with an address to submit a letter of dispute.
- Apply for fewer loans and credit cards. Applying for several loans or credit cards in a short period of time can make you appear financially desperate and significantly lower your credit rating.

- Pay off your credit card balances or at least pay off enough so the balance is 50 percent or below your available credit limit. If you have sufficient equity built up in your home, you can refinance or take out a home equity loan to pay down your credit card debt.

TIP

For additional tips on boosting your credit score, check out *Credit Repair Kit For Dummies* by Stephen R. Bucci and Terry Savage (Wiley).

Gathering the paperwork and records you need

Prepare in advance for your meeting with your bank or mortgage broker. Call and ask for a list of documents and records they need, and make copies to bring with you to your first meeting. Most banks and mortgage brokers typically require the following documents:

- Two or three recent pay stubs showing your income
- Your two most recent federal income tax returns
- Your two most recent bank statements
- Recent loan statements that show how much you currently owe on your car, credit cards, or other purchases you've had to finance

TIP

If your net-worth statement shows that you own much more than you owe, bring it along, too. Banks and mortgage brokers like to see people who have a positive net worth, know the importance of net worth, and care enough to monitor it.

Comparison Shopping for Low-Cost Loans

Your bank or mortgage broker is likely to lay out a virtual buffet of loan types from which to choose: fixed-interest, adjustable-rate mortgage (ARM), interest-only, balloon-payment, and others. For details on the benefits and drawbacks of these various types of loans, ask the bank representative or your mortgage broker lots of questions.

TIP

Don't get too caught up in the various types of loans. For people who are buying houses they plan to reside in for 30 years, loan type is a big consideration. For real estate investors who plan on buying and selling the property in less than a year, the cost of the loan over the life of the loan becomes more important. To compare loans, take the following steps:

1. **Start with the amount the bank charges you up front in loan origination fees, discount points (interest you pay up front, typically a percentage of the loan, to lower the interest rate), and other fees.**
2. **Multiply the monthly payment times the number of months you plan to pay on the loan.**
3. **Add the two amounts to determine your total payment.**
4. **Total the amount of each payment that goes toward paying the principal of the loan.** (Your lender can tell you how much of each payment goes toward principal.)
5. **Subtract the total you determined in Step 4 from the total in Step 3.**

Say that you're considering two loans, each for $100,000. You plan on using the loan to buy and renovate a home over two years and then sell it and pay off the remaining principal on the loan. You have a choice between a 30-year, fixed-rate mortgage at 6 percent or a 30-year, interest-only loan at 5 percent. Look at the 6 percent, fixed-rate mortgage first:

Loan origination fee and discount points:	$1,000.00
Plus monthly payment of $599.55 × 24 months:	$14,389.20
Equal total payments:	$15,389.20
Minus total paid toward principal:	$2,531.75
Equal total cost of loan:	$12,857.45

Here are the numbers for the 30-year, interest-only loan at 5 percent:

Loan origination fee and discount points:	$1,000.00
Plus monthly payment of $416.67 × 24 months:	$10,000.08
Equal total payments:	$11,000.08
Minus total paid toward principal:	$0.00
Equal total cost of loan:	$11,000.08

As you can see, even though you're not paying down the principal on the interest-only loan, over the life of the loan, you pay about $1,700 less. In addition, the interest-only loan has much lower monthly payments, freeing up cash to use for renovations and other investments.

TIP

As a general rule for quick flips (buying and selling a property in less than six months), opt for loans with low (or no) closing costs, low (or no) discount points, and low interest rates. Avoid any loans that have early-payment penalties.

Chapter 6

Networking Your Way to Foreclosure Success

In This Chapter

- Generating quality leads through networking
- Making yourself the go-to guy or gal
- Marketing yourself as a foreclosure investor
- Optimizing the storage and retrieval of good contacts
- Taking care of the people who take care of you

As a real estate investor, you can't climb very far up the ladder of success on your own. You need access to cash, leads on potentially profitable properties, information about those properties, guidance from more experienced investors, legal and financial advice, referrals to affordable contractors and handymen, and much more. You need assistance, and the best way to get that assistance is through networking.

In this chapter, I unveil the power of networking and reveal techniques and tips that can transform a lone wolf into a well-connected real estate investor. By mastering the techniques in this chapter, you can reduce your workload and streamline the process of buying, renovating, and selling foreclosure properties.

Grasping the Power of Networking

I owe much of my success as a real estate investor to the advice, assistance, and resources of thousands of people. These individuals generously donate their time and expertise to provide me with the financing and high-quality leads I need to succeed at investing in foreclosures and other real estate. Without the guidance and support of thousands of people, I would never have experienced the level of success I now enjoy.

I strongly encourage you to take the same approach when you're first starting out and for however long you continue to invest in real estate. In the following sections, I reveal the benefits of networking in all aspects of foreclosure investing.

Today, right now, start building a strong network. Every business day, I make 100 phone calls and send another 150 e-mail messages to keep in touch with clients, colleagues, distressed homeowners, and a host of others who need my assistance and who assist me. I'm not saying you need to make 100 calls per day. Start slowly with 3–5 new contacts a day, and then work your way up. Every person you contact probably knows about 250 other people, many of whom may eventually need your help or who can help you. Over a short period of time, your network begins to grow exponentially and almost effortlessly. Think of it this way, if business is slow, turn *not*working into *net*working and you will have more business than you can handle.

Generating leads on profitable pre-auction properties

The earlier you step into the foreclosure process, the greater your chances are of eventually taking possession of a property, and the earliest you can find out about a foreclosure is through word-of-mouth leads. Distressed homeowners, knowing that you buy foreclosures and have a reputation for being fair, may call you out of the blue to buy their property. Maybe someone you know knows someone who knows someone who's currently facing a financial crisis. Or perhaps another investor you know is too busy or doesn't have the funds available to follow up on a golden opportunity.

Networking delivers people and property to you, saving you from having to do the legwork to track down potentially profitable properties. Everyone you meet is a potential lead generator — attorneys; real estate agents; mortgage brokers; title company staff; loan officers; contractors . . . even the person delivering your mail or your pepperoni pizza. Let everyone know that you can help homeowners who are facing financial crises. You may have secrets, but what you do and what you want to do shouldn't be one of them. Tell everyone what you do!

For details on how to network effectively to find foreclosure properties, skip ahead to Chapter 7, where I provide a list of the top people to contact for leads.

Discovering opportunities in divorce

Divorce frequently orphans properties. A couple splits up, neither the husband nor the wife can afford the monthly mortgage payments on their own, and they're forced to sell their home.

When a divorce attorney gets involved, the couple has even less money to pay the mortgage. In many cases, the wife or husband or both use the home as collateral to pay their attorneys out of the proceeds from the property settlement. The attorney often works unpaid until the property sells, so the attorney places a lien on the property to secure payment. Many divorce attorneys have liens on several properties, and they don't get paid until those properties sell.

You can profit from these situations in two ways. First, by networking with divorce attorneys, you may find attorneys with clients seeking to sell their homes prior to auction.

Another way to profit is to negotiate a short sale with the divorce attorney. Say the wife receives the home as part of the divorce settlement and starts missing mortgage payments, so the bank initiates foreclosure proceedings and posts a foreclosure notice. You're trying to buy the property from the wife, but if you paid what she's asking, you wouldn't profit. The house has a lien on it for $8,000 from the husband's attorney, because the husband used the house as collateral to pay his attorney. You could show the foreclosure notice to the husband's attorney, explain that his $8,000 lien is going to be wiped out by the foreclosure, and ask if he'd be willing to take $1,500. That way, the attorney gets something out of the deal, you save $6,500 on the purchase, and you can afford to offer the wife a little more for the house.

Short sales are a great way to turn an unprofitable purchase into a profitable one. For more about short sales, check out Chapter 15.

Securing your financing

Need money? Maybe all you have to do is ask for it. Securing financing may not be quite that easy all of the time, but it can be some of the time. If people who have plenty of money lying around know that you have a proven track record for making money, they may rather invest in you than bet their money on stocks and bonds or entrust it to a financial advisor.

TIP

Network with the hard-money lenders in your area — local banks, mortgage companies, and private lenders. You may make these contacts at real estate investment clubs, while you're doing your personal banking, through your mortgage broker, or as you network with other real estate professionals.

WARNING!

When borrowing money from private lenders, be careful not to present the transaction as something other than a personal loan. If you pitch the deal as an investment opportunity, the loan may fall under SEC (Security and Exchange Commission) guidelines for investors. You can borrow money from family and friends as a personal loan, but if you plan on establishing a relationship with the lender as an investor, work through a mortgage broker. Consult with your attorney to make sure you're doing everything correctly and above board.

Tracking down reliable, affordable professionals

Without networking, you're working in a vacuum whenever you hire an attorney, accountant, agent, title company, inspector, or contractor. Other people in your area are fishing the same pool, and they've already scoped out the best fishing holes. Don't waste your time flipping through the phone book for top-notch professionals. Word-of-mouth referrals are the way to go.

TIP

Real estate agents are in the business of assisting people with all issues related to buying, owning, and selling homes. They often have a fat address book that's packed with valuable contacts for other agents, attorneys, title companies, home inspectors, accountants, and contractors. They know the power of networking and are typically more than willing to recommend people, especially if you tell the people you call who recommended them.

Selling your house for more money in less time

When real estate agents place a house on the market, they essentially network to find interested buyers. Sure, they may create full-color flyers and brochures and plant a For Sale sign on the front lawn, but they connect to most prospective buyers using a networking tool called the MLS (Multiple Listing Service). When a seller works through an agent, the agent posts the listing on one or more MLS. Buyers' agents can then pull up these listings to find houses for their clients. The top agents also network with large companies that have relocation divisions.

In Chapter 19, I strongly recommend that if you decide to sell your foreclosure property, you work through an agent who has access to all of the multiple listing services in your area. Using the MLS enables you to tap the power the most powerful networking tool for selling the property quickly and for top dollar.

You can generate additional interest in your property through your own network. Before you list the property, start talking about it. Inform everyone you know in the area that you have a property you're fixing up that promises to be spectacular. Everyone you tell potentially knows a friend, relative, or colleague who's thinking of moving to the area. The person you tell may just be the one who delivers a buyer right to your front door! Consider creating a business card specifically for a single house you're selling and pass it out to everyone. You can get a box of 1,000 cards very reasonably, and it works.

Realizing the Importance of Being Good

As the old saying goes, "News travels fast. Bad news travels faster." You can take months building a support network, but if you start doing shoddy work, stealing houses from financially strapped seniors, or transforming neighborhoods into slums, your support network is likely to turn into an angry mob that would just as soon see you tarred and feathered and run out of town.

Every foreclosure property you buy, renovate, and sell is a reflection of you and how you do business. Build a strong reputation by treating everyone you meet fairly and with respect. When you renovate a property, make the house a home you would be proud to put your name on. Work to improve the housing in the community where you do business. I usually have more opportunities to acquire properties than I can reasonably follow up on, so I have to rule out some prospects. I ask myself, "After I get the place all fixed up, could I envision myself living here?" If the answer is "No," I cross it off the list.

Acting with integrity — always

People are generally pretty willing to trust others. Only after they're disappointed do they form a negative opinion. In short, your good reputation is yours to lose or improve.

You wouldn't recommend a restaurant to a friend if the food was bad, the service was lousy, and everything on the menu was overpriced. The same is true in real estate. By building a reputation as a straight shooter who plays by the rules, you become the person to whom others steer their business. This doesn't mean that you have to be kind to the point of giving away all your profits — it simply means telling the truth, fully disclosing your intentions, following through on promises, and doing high-quality work.

Investing in quality craftsmanship

Homeowners as well as real estate investors often try to boost their bottom line by hiding defects in a property. Instead of repairing a leaky foundation, they install wood paneling over the weeping walls and run a humidifier to take out the "dampness." Rather than repairing the termite damage in the floorboards, they lay wall-to-wall carpeting. They try to hide the foul odors by creating an aromatic cloud of potpourri.

When repairing and renovating a home, your goal should be to bring the home up to market standards. I'm not saying that you need to transform a Quonset hut into the Taj Mahal. If you're renovating a foreclosure property in a low-rent district, using builder's grade materials instead of top-of-the-line stuff may be sufficient. Hiding defects in a property, however, can come back to bite you in the seat of your pants. Once the homeowners discover the defect, they're liable to come back to you, and if you don't immediately rectify the situation, you may be dragged into court or worse — they may start telling all their friends, family, and neighbors that you ripped them off!

For details and tips on how to affordably renovate a home without cutting too many corners, see Chapter 17.

Building thriving communities

Neighborhoods, especially the most profitable neighborhoods, like to see investors come in and clean things up. When you transform the neighborhood eyesore into an attractive abode, you not only make the neighbors feel better about where they live, but you also improve their homes' values. You gain your own personal sales force of enthusiastic supporters who spread the good word about the new house on the block that's up for sale.

Some investors who are just out for the quick buck buy a property, cash out the equity, and quickly lose interest in it. Con artists may even use the house for some illegal flipping scheme, paying an appraiser to inflate the home's value, cashing out the inflated equity, and then abandoning the property altogether. Don't join the ranks of these real estate leeches.

WARNING!

Don't get seduced by quick cash opportunities. In the long run, you stand to make much more money investing in foreclosures by being sincerely interested in the neighborhoods you're investing in. When con artists descend on a neighborhood like a swarm of locusts and leave it devastated, they earn a quick profit, but they also earn the loathing of the neighborhood. When you work to improve a neighborhood, you build a neighborhood that's ready and willing to support you.

Marketing Yourself

Productive networking requires some proactive efforts on your part, especially when you're first starting out. People are often ready, willing, and able to assist an honest and competent investor if they know that such a person exists. By marketing yourself, what you have to offer, and what you need to do your job, you soon discover that your name, face, and reputation are recognized throughout the neighborhood.

To market yourself effectively, assemble your marketing toolkit, and then get busy talking, calling, e-mailing, and mailing out notices to let everyone know what you do, what you offer, and what you need. In the following sections, I show you how to effectively market yourself as a foreclosure investor.

Gathering your marketing tools

You don't need to hire a public relations firm to market you as a foreclosure investor. All you have to do is gather a few basic tools and get to work. You probably already have most of the marketing tools you need, as described in the following sections.

TIP

Field research I've performed (by attending weddings and funerals) reveals that every individual knows about 250 other people. When you impress one person, you have the opportunity to impress at least 250 others. Word of mouth is the most powerful networking tool.

Designing and printing business cards

Even in this hi-tech age of computers, Web sites, and cell phones, the lowly business card is your key marketing tool. If you have a computer and a fairly good printer, you can design your own business card and print it on card stock that you can pick up at any office supply store in your area. If you don't have a computer and printer, head down to the local print shop to have it produce your cards. Include the following on your cards:

- A cameo shot of yourself, so people know your face.
- Your name and business name, if you have a business.
- Your mailing address. Don't use a post office box number — it's too impersonal, and nobody will trust you. People trust brick-and-mortar establishments.
- Your phone number.

- Your e-mail address and Web site address, if you have one.
- A statement of what you do — for example, "I Buy Houses for Cash."

TIP

Pass your card out to everybody you meet, and I mean *everybody.* If you step into the local burger joint for lunch, hand your card to the server or the person behind the counter and say, "Hey, I buy houses for cash if you ever know of anybody . . . ." You'd be amazed at how many people know a homeowner who's embroiled in a financial crisis.

Buying yourself a cell phone

Homeowners facing foreclosure are usually in desperate situations, and they need help yesterday. You want to be the person they can contact in their hour of need, so if you don't have a cell phone, buy one now and carry it with you 24/7. Every missed call is a missed opportunity.

WARNING!

You can usually get by with a single cell phone for both business and personal use, but if you have to carry a cell phone for work, and your boss is paying the phone bill, I discourage you from using that cell phone to moonlight as a foreclosure investor. Unless your boss is okay with it, buy a separate cell phone. The same goes for doing research when you're supposed to be working and using your boss's computer to do it.

Equipping yourself with a computer

Nowadays, a computer is a necessity in all areas of real estate. Before you venture out into the world of foreclosures, equip yourself with a decent computer, an Internet connection with e-mail, and a printer. Your computer is an essential tool for performing the following foreclosure investing tasks:

- Researching state and county foreclosure laws and regulations
- Finding and researching foreclosure properties
- Keeping in touch with contacts via e-mail
- Designing and printing your own marketing materials
- Establishing a Web presence for additional leads
- Shopping and applying for loans
- Managing your finances, if you choose to do your own accounting

Creating ads

I recommend against advertising yourself in the local newspaper as a foreclosure investor until you're well established and have a strong enough financial base to buy and hold multiple foreclosure properties.

After you're well established, however, you can generate additional leads on pre-auction properties by placing a small add in the classifieds that says something like, "I Buy Homes for Cash," followed by your phone number. For details about advertising for leads, see Chapter 7.

Starting with your inner circle

The most challenging step in networking is often the first step. You may simply not know where to start. The best place to begin is with your inner circle — family, friends, and co-workers. Tell them your plans, brainstorm for additional ideas, and try to find out if they know anyone who may be able to assist you — real estate agents, attorneys, loan officers, bankers, local officials, and so on.

Whenever you work with a mortgage broker, title company representative, or other real estate professional, ask if she knows anyone else who may be able to help. Take names and phone numbers, even if you don't need a certain person's expertise right now. You may find that the person can offer assistance somewhere down the line.

When networking with your inner circle, avoid the dream killers, especially family members who don't believe in you. These confidence busters can often convince you to give up long before you buy your first foreclosure property. Only you know what you're capable of accomplishing, and often times you don't even know until you've accomplished your goal.

Start at the top. Referrals tend to work from management to employees rather than moving in the other direction. If your friend is a car salesman, he can refer you to his employees, to the porter, to the clerical staff, and so forth.

Keeping in touch . . . a daily chore

When's the last time you called your best friend from grade school? If it was more than about a year ago, chances are good that you'll never touch base with that person again. The same is true in business, but the time is shorter. If you lose touch with a valuable contact for more than a month or two, that person is going to quickly forget you ever existed.

I have a database of more than 6,000 people and growing whom I assist and who assist me in my various business dealings. Every day, I personally contact nearly 250 people over the phone and by e-mail, which keeps my name and face in the minds of the people I rely on.

TIP

Harvey Mackay, motivational speaker and author of *Swim with the Sharks,* taught me some of the most valuable lessons I've learned about sales. Harvey said he made sure he knew at least 66 things about every one of his customers. This sales tactic applies to networking, as well. Try to find out 66 things about every person you contact — their birthday, anniversary, spouse's name, kids' names and ages, hobbies, interests, and so on. You don't have to find it out all at once — slowly gather details over time. The more you know about a person, the more you can become genuinely interested in their lives, and the stronger the bond you can establish with that person.

Managing Contact Information

Don't rely on memory alone or a purse stuffed with scraps of paper to keep track of all the people in your network. Use a contact management program or database to record all the pertinent and not-so-pertinent information about each individual.

TIP

I use Outlook, because it enables me to enter the names, addresses, phone numbers, and e-mail addresses of everyone I know. Outlook's robust features offer several additional benefits:

- Record the person's birthday, anniversary, and spouse's name
- Type in additional notes about the person's family, interests, and specialties
- Remind you of important dates and activities, so you can contact the person on key dates
- E-mail multiple people with a single e-mail message
- Synchronize contact information from your computer to your PDA (personal digital assistant), so you can take your contact information on the road

For more about using Outlook, check out *Outlook 2007 For Dummies* by Bill Dyszel.

You don't have to use Outlook. Prior to using Outlook, I used a program called ACT to manage my contact list. (I still use ACT to track foreclosures.) The important point here is that you record contact information using a tool that provides you quick access to that information. You can even use a word processor, spreadsheet, or database program, a PDA (Personal Digital Assistant), or a day planner or address book. Figure out a system that works for you.

Adding that personal touch

By storing personal information about each individual in your contact management program, you can easily call up specific details about an individual that you may not recall.

Before I place a phone call, I pull up the person's contact information and review it. It's pretty cool when you get Bill on the phone and you say, "Tell your wife, Debbie, I said, 'Hi,'" or you call Bill's house, Debbie answers, and you say "Hi, Debbie, this is so-and-so, is Bill available?" Later, when Bill comes home, Debbie tells him, "You know, so-and-so called, and he knows *my* name. He probably talks to thousands of people, and he remembers *my* name." That means a lot to most people.

Even though I have a pretty good head for names and dates, I often forget. When I call Bill, I usually don't remember Debbie's name, but I look it up before I call. In fact, just before calling my house, I look up my contact information in Outlook, so I remember my wife and kids' names. Since I have been using Outlook, I have not made a mistake or missed our anniversary or my wife's birthday.

Don't count on memory alone.

Rewarding Good Deeds and Good Leads

When you're asking for guidance, assistance, and good leads, be prepared to reward the helping hands who assist you. People quickly forget or even worse, become resentful, when others constantly ask for assistance and forget to demonstrate their appreciation in some tangible way. To expand your network, show your appreciation. Here are some suggestions on what you can do to keep the people in your network happy and reach out to others:

- Refer other people to your agent, attorney, mortgage broker, title company, contractor, handyman, and other professionals who've provided excellent service. Ask for extra cards, carry them with you, and pass them out. A referral is the highest form of flattery.
- When you contact someone you've been referred to, let the person know who referred you.
- Treat everyone you encounter — from your real estate attorney to the person who's repairing the leaky faucet in the home you just bought — with sincere respect. If you value others, they value you.
- When someone helps you, show your appreciation by sending them a quick, handwritten note. People have different needs, but everyone needs to be thanked.

- Keep an ear to the ground for people in your network who need your assistance. If they're in trouble, a random act of kindness with no thought of what you'll eventually receive in return demonstrates that you're genuinely interested in their success.

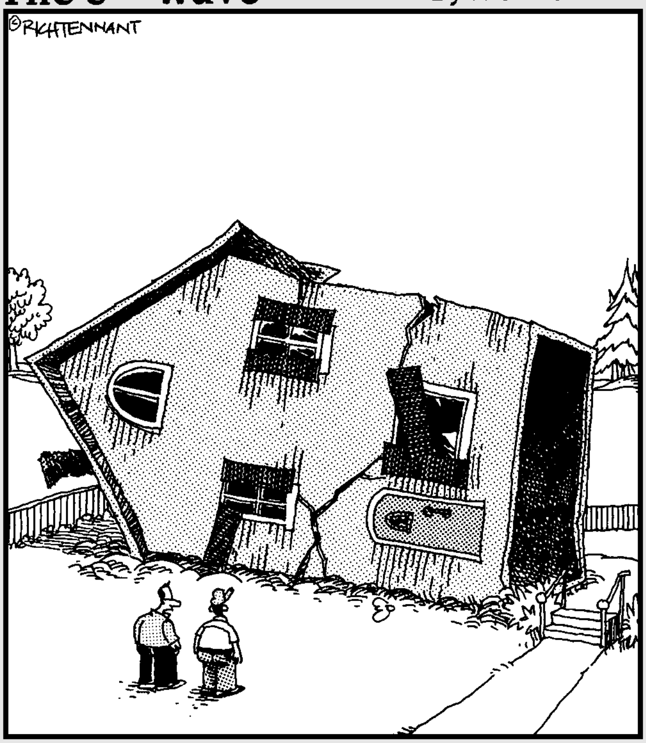
TIP

Give back to the community. Think of networking as a ladder with you standing on one of the middle rungs. Above you are more experienced people who can reach down and pull you up. Below are less experienced people you need to reach down to. You never stop learning, and once you learn, you have the obligation to teach.

Part III

Creating Win-Win Situations in Pre-Foreclosure (Prior to Auction)

The 5th Wave By Rich Tennant



"What if we put the solid granite Jacuzzi on the first floor?"

In this part . . .

Ending up in foreclosure can be an emotionally devastating experience for homeowners, but by guiding them through the process and honestly, openly laying out their options to them, you can often help homeowners while profiting from pre-foreclosure transactions.

The chapters in this part show you how to step into the foreclosure process at the possible earliest stage to reduce competition from other investors and provide the most useful and timely advice to distressed homeowners.

Here you discover how to locate properties before they end up on the auction block, gather essential information about those properties and their owners, and assist homeowners through the foreclosure process while acquiring properties well below their market value.

Chapter 7

Discovering Homeowners Facing Foreclosure

In This Chapter

- Plugging your ear into the neighborhood grapevine
- Advertising for additional leads
- Cruising the neighborhood for disheveled or abandoned properties
- Checking out properties for sale by owner
- Finding and deciphering foreclosure notices

The earlier in the foreclosure process you contact distressed homeowners, the better chance you have of helping them claim some of the equity they've built up in a property while snagging a property that's worth your time and effort.

But how do you track down distressed homeowners early in the process? You can take any of several approaches. My personal favorite is through word-of-mouth networking, because it often delivers the most timely information. But you can also discover opportunities by cruising the neighborhood for unkempt homes or homes that are for sale by owner (FSBO), searching and advertising for properties online, and perusing the county legal news for foreclosure notices.

In this chapter, I show you exactly what to do to locate distressed homeowners prior to auction — before it's too late in the foreclosure process to assist them.

TIP

In Chapter 8, I show you how to gather the information about the property and the homeowners that you need to provide the homeowners with the assistance they need, and in Chapter 9, I reveal tips and strategies for personally contacting the homeowners, so you can discuss their situation and their options.

Networking Your Way to Promising Properties

Before the foreclosure notice is posted and the foreclosure becomes public knowledge, you have only two ways of finding out that the homeowners are in a jam and need to sell their home in a hurry:

- **Word-of-mouth networking:** You hear of someone who needs your assistance or a distressed homeowner hears of you.
- **Must-sell ads:** You notice an ad in the classified section of the local newspaper that conveys a sense of duress. Look for ads that say "Must Sell" or "Relocating." These ads often clue you into the fact that the owners must sell in a hurry and are possibly in jeopardy of losing their home.

In Chapter 6, I reveal some basic networking strategies to obtain the assistance you need and to get the word out about what you do. In the following sections, I go into more depth, as I list the people who are often the source of the best leads on foreclosure properties.

Identifying your personal lead generators

A *lead generator* is anyone or anything that can steer distressed homeowners your way or point you in the direction of distressed homeowners. It can be a banker, real estate broker, loan officer, divorce attorney, the minister of your church, a casual acquaintance, a classified ad, a Web site, or an Internet bulletin board on which you post a notice.

Dealing with an embarrassing situation

When homeowners are in a dire financial situation, they often go mute, telling nobody, not even their family or closest friends, what's going on. In some cases, they contact a lawyer or tell the minister at their church or a counselor or therapist or even a complete stranger. If they know that you assist homeowners who are financially strapped, they may tell you.

If the distressed homeowners remain uncommunicative, you have no chance of finding out about the situation until the foreclosure notice is posted. If they tell someone, your chances of hearing about it increase in direct proportion to the number of people who know that you assist distressed homeowners.

As a professional and someone who's not intimately involved in the situation, the homeowners may be more willing to talk with you, especially if you act professionally and have the confidence that you can assist them with overcoming their problem.

In the following sections, I list the human lead generators you can often rely on to identify foreclosure opportunities in your market.

TIP

People who know you personally are the best lead generators because they act as mutual friends, referring and recommending you to homeowners they know. Keep in mind that when someone refers you to one of her friends or acquaintances, that referral reflects on the person who gave it. Earn that person's trust by treating the homeowners with respect and doing everything possible to assist them in their time of need.

Creating your A-list

Real estate professionals and attorneys who specialize in certain areas can feed you some of the most productive leads. These are your A-listers:

- **Foreclosure attorneys:** Foreclosure attorneys post the foreclosure notices and handle the liquidation of properties. You should know all the foreclosure attorneys in your market by name and have their phone numbers and e-mail addresses at the top of your A-list.
- **Real estate attorneys:** The real estate attorneys in your area know the market and the foreclosure rules and regulations and are often in contact with distressed homeowners. In addition to providing you with leads, real estate attorneys often provide some excellent advice. Pick their brains for additional information.
- **Divorce attorneys:** When couples divorce, they often no longer can afford the house they purchased together. In many cases, the divorce settlement requires that they sell the house and split the proceeds, and divorce attorneys often want this to happen as quickly as possible, so they can get paid.
- **Bankruptcy attorneys:** Bankruptcy often requires the homeowners to sell their real estate in order to restructure their debt. Bankruptcy attorneys frequently need to work with investors who can close on the deal in a hurry. Few, if any, of the bankruptcy attorneys I know buy real estate. They do their thing and would love to have an investor in their network to purchase properties.
- **Probate attorneys:** When a homeowner dies, leaving behind a home or other real estate, the home must be liquidated and the proceeds divided among the heirs. When settling an estate, probate attorneys often rely on investors who can pay cash for properties to expedite the process.
- **Loan officers:** Loan officers specialize in working with people who have bruised credit and refinancing homeowners out of foreclosure or bankruptcy. In many cases, the loan officer can't help the homeowners and needs an investor to step in and purchase the property. By networking with loan officers, you can become their go-to investor.
- **Homeowner associations:** Condominium and homeowner associations are sometimes empowered to foreclose on homeowners who don't

properly maintain their properties or don't pay their association dues. When homeowners in the association encounter financial problems, the association may hear about it before the foreclosure attorney posts a notice. The association may agree to pass your name and contact information along to homeowners who need to explore their options.

You should also network with REO (Real Estate Owned) brokers — real estate agents who the banks call on to sell the properties they repossess. They may not be able to provide leads on pre-auction properties, but they can offer leads to great post-auction opportunities. For more about working with REO brokers, see Chapter 12.

Contacting friends, family, and neighbors

When you're shopping for a car, you ask a dealer or a mechanic for advice. When you're in the market for a diamond ring, you ask a jeweler. In the same way, when you're looking for foreclosure properties, your best leads often come from real estate professionals, because they specialize in the housing market where you invest.

In the case of foreclosures, however, real estate professionals are not your only lead generators. Family members, friends, and neighbors often know about homeowners who are having financial problems long before word reaches the real estate community. Tell family members, friends, and neighbors that you provide assistance to distressed homeowners. If the people closest to you don't know that you provide services to help homeowners in crises, they won't even think of telling you or referring their friends to you.

Building on your church affiliations

Churches exist primarily to meet the spiritual needs of their congregations, but they also function as community centers to assist members with relationships, raising children, and financial matters. Some homeowners feel more comfortable telling their ministers or other church members about their financial woes than they are breaking the bad news to their spouses.

I'm not telling you to join a church solely to tap its membership for leads, but if you already belong to a church or are thinking of joining one, the church can be an additional lead generator, and you can often assist members when they don't know where else to turn for help.

When an entire area suffers a serious financial blow, such as mass layoffs or a major employer moving out of the area, consider holding a meeting at the church to inform homeowners in the congregation of their options and foreclosure rights. You may do more good than you could ever imagine.

Networking through clubs and other organizations

Do you belong to any clubs in your area — the Rotary Club, Kiwanis, the Elks, the Moose, the Legion, the Lions Club, the Purple Hatters? If so, don't forget to mention to your fellow members that you assist distressed homeowners.

You never know when a fellow member may be facing some financial hardship or knows a homeowner who's in a financial pickle. By letting others know what you do, you give them someone they can approach to ask questions or seek assistance. And don't forget to hand out your business cards, as explained in Chapter 6.

Close your eyes and try to picture your spouse, your child, your favorite pet, or the first President of the United States. Chances are good that you have a pretty clear image of that person . . . or dog, or cat, or hamster in your mind. By telling everyone that you assist distressed homeowners and buy properties, you begin to create an image in their minds that you're the go-to guy or gal whenever they or someone they know is about to lose their home.

Getting the word out on the streets

Unless you wear blinders while driving around or flipping through the local newspaper, you've probably noticed billboards or ads that say stuff like "We Buy Ugly Houses" or "Need Cash? We Buy Houses!" or "Foreclosure? We Can Help."

The people who post these ads are investors, just like you, fishing for early leads on pre-auction properties. They're usually pretty well-established investors who have plenty of money and resources on hand to field all the calls they get.

Don't post an ad or paint your name and phone number on a billboard until you're capable of handling numerous phone calls. Advertising before you're prepared can backfire on you and ruin your reputation in the community as the resident champion for the distressed homeowner. When you're first starting out, focus on fewer properties, so you can devote all of your energy, expertise, and resources to doing an outstanding job. Later you can think about advertising.

You can also advertise online on sites such as Craig's list at `www.craigslist.org` or create a blog on MySpace.com at `www.myspace.com`. Some real estate investment groups also have their own bulletin boards on which you can post messages asking for financing or for leads on investment properties. Just don't forget to do your due diligence — con artists often prowl sites looking for suckers.

Scoping Out the Neighborhood for Dontwanners

In my book *Flipping Houses For Dummies* (Wiley), I encourage real estate investors to cruise their neighborhoods looking for *dontwanners* — properties that the owners don't want so much that that they're willing to do anything to get rid of them, including offering their homes for sale at a deep discount.

Dontwanners are especially relevant when investing in foreclosures, because homeowners who are strapped for cash typically don't have a budget for home maintenance. Some homeowners even pack up and move out, abandoning the house altogether. By knocking on the door and talking to the homeowners and neighbors, you may just stumble on a property with residents who are in the very early stages of foreclosure.

Although word-of-mouth networking is often the best way to track down pre-auction properties, don't focus so much on networking that you overlook some prime real estate opportunities that you may be driving past on a daily basis. Keep your eyes peeled for the dontwanners in your market. Here are the common signs of a dontwanner:

- Newspapers stacked on the front step
- Neglected lawn
- House looks vacant — lack of furniture inside, no window blinds or curtains

If you spot a dontwanner, talk to the neighbors to find out who owns the house, and then try to contact the owners to see if they want to sell the house. Sometimes the owners are so fed up with a property that they're not even willing to take the time and trouble to place it on the market.

TIP

To gather inside information about the property, contact the owners. If you can't find out who owns the property, head to your county's Register of Deeds office and ask to see the title. For more about researching a property, check out Chapter 8.

Searching for FSBO Properties

One of the smartest actions a homeowner can take when they find themselves in a financial hole they can't dig themselves out of is to sell their home and move into more affordable accommodations. To save money, they may try the FSBO (for sale by owner) route, so they don't have to pay the standard 6–8 percent real estate commission. This approach, however, often backfires, because selling a home without the assistance of a real estate agent isn't all that easy. The homeowners may find that they have few interested house hunters or they don't have the money to fix the house up to make it marketable, and the house lingers on the market while their financial hole deepens.

Of course, FSBO sellers aren't always experiencing financial hardship, but you never know until you knock on the door, take a look around, and talk with the homeowners.

You can locate FSBOs by driving around the neighborhood and looking for "For Sale" or "For Sale By Owner" signs. These are usually the cheaper looking For Sale signs that you can pick up at your local hardware store, pen in your phone number with a permanent market, and poke into your front lawn.

TIP

Another way to locate FSBOs is to check any of the many for-sale-by-owner sites on the Web. One of the more popular sites is cleverly called ForSaleByOwner.com at `www.forsalebyowner.com`. You can find additional sites by pulling up your favorite Internet search tool and searching for "for sale by owner." Look for keywords in the listing, such as "fixer-upper," "needs work," "foreclosure," or "must sell." I mention FSBO sites only because they may lead you to opportunities. I advise against subscribing to any sites that specifically sell foreclosure listings. I've subscribed to "exclusive" listings in the past that have included homes I had already purchased at a sale. In other words, the listings are often useless.

Finding Foreclosure Notices

I take the foreclosure notice as somewhat of a personal failure. I wonder, "Why didn't this homeowner come to me first?" The foreclosure notice marks the beginning of the end — the day when the lender first publicly announces that the homeowners haven't been making their payments. It's also the day when foreclosure investors ramp up their efforts to contact the homeowners and when con artists often begin crawling out from under their rocks or whatever dark place they choose to hide.

Even though the foreclosure notice marks the beginning of the end for most distressed homeowners, it usually appears several weeks prior to the auction, so you still have a little time left to assist the homeowners. Also, if the house does end up on the auction block, the foreclosure notice provides you with additional information you can use to start tracking the foreclosure, so if the opportunity arises for you to purchase the property later, you can be well prepared in advance with the information you need to make a good purchase decision.

Tracking down local publications

When a lender initiates foreclosure proceedings, the lender posts a foreclosure notice or Notice of Default (NOD) in the county's legal newspaper or the local newspaper. Contact your county's Register of Deeds office and ask where they post foreclosure notices.

Visit your county's Register of Deeds office and get to know the staff. While you're there, see if they have an extra copy of this week's county legal news. They may have a rack of them sitting near the desk or just outside the office. Pick one up, head to your local coffee shop, and read through it from cover to cover.

If you live in a county that sees a fair share of foreclosures, the foreclosure listings can seem overwhelming at first. You skim page after page of listings written in legalistic gobbledygook. The trick to making the listings less cumbersome is to know what you're looking for and then weed out any listings that raise red flags. For example, if you find a property on Main Street with a mortgage of $200,000, and you know of no property on Main Street that you'd pay more than $150,000 for, you know that property isn't for you. If the same property is listed for $75,000, it may be worth investigating.

Getting on the mailing list

Whoever publishes your county's legal news is likely to have a subscription service, so you can have the publication delivered to your door or sent to you electronically via e-mail. In some counties, you can view foreclosure notices online at the Register of Deeds Web site for free.

Ask one of the staff members at the Register of Deeds office about your options or search this week's edition of the county legal news for information about subscribing.

Your county's legal news is not recommended reading — it's required reading. Carefully read through the foreclosure listings every single week, and keep track of every property that catches your eye. You may notice that a notice for a property one week does not appear the following week, indicating that the owners may have worked out a forbearance with the lender or received an adjournment. Keep following the property to see if it appears again. Properties often disappear from the radar only to reappear weeks or months down the road. In Chapter 8, I explain how to create a database for tracking properties.

Subscribing to commercial foreclosure information services . . . or not

You can find plenty of commercial services that deliver foreclosure notices via e-mail, snail mail, or through member-only Web sites. Some of these services charge fees that are fairly reasonable — you can buy notices by city, county, or zip code to keep costs down. Other services may charge $3,000 a year to mail you notices that are out of date by the time the mail carrier delivers them.

WARNING!

Don't waste your money on high-cost foreclosure subscription services, and never rely solely on a commercial subscription service for leads. These services are no replacement for reading the weekly county legal news. Why pay more for a commercial service when your county provides the same or better information for free or for a modest subscription fee? If you decide to subscribe to a service, sign up for your own zip code first and test it out. Compare the results to your own research to see if the information is timely and accurate. Most of these services offer dated material, but sometimes they provide valuable leads.

TIP

Another great place to research foreclosures, FSBO (For Sale By Owner) properties, pre-foreclosures, and bank-owned properties is HurryHome.com at `www.HurryHome.com`. In addition to providing you with a handy online tool to search for properties, HurryHome.com features neighborhood profiles, recent home sales data, and unlisted real estate. Another useful site to check out is `www.GuthyRenkerHome.com`), where you can also find some excellent articles on real estate topics.

Deciphering a foreclosure notice

Attorneys write foreclosure notices, so you can expect them to be written in cryptic legalese that seems to discourage the average person from thinking about buying the property. In Chapter 8, I present a sample foreclosure notice that shows just how cryptic they can be, and I highlight the important pieces of information the foreclosure notice contains:

- File number
- Foreclosure attorney's name and contact information
- Liber (the legal book in which the deed is recorded at the county courthouse) and page number of the mortgage

- Mortgagors' names (who owes the money)
- Lender's name (bank or mortgage company)
- The amount that remains to be paid on the loan
- The interest rate
- Legal description of the property
- Length of the redemption period, if any
- Whether this is the first, second, third, or fourth posting of the foreclosure notice

Hurry. The clock's ticking. You have about 30 to 90 days from the time the foreclosure notice appears in the paper before the property goes on the auction block. You also have more competition now that the foreclosure is public knowledge. Head to Chapter 8 and start gathering information about the property pronto!

TIP

After you find a property in which you're interested, double-check to make sure that it's going to be sold. Sometimes, the foreclosure notice is posted, and then the homeowner files for bankruptcy or takes some other action to cancel or postpone the sale. Call the attorney listed in the foreclosure notice, introduce yourself, and find out everything you can about the property. You may be able to obtain additional information from the attorney, such as the opening bid and when it's scheduled for sale, but don't count on it — the attorney is acting as a debt collector on behalf of the lender.

Chapter 8

Building a Property Dossier

In This Chapter

- Investigating a foreclosure property's vital statistics
- Gathering legal documents at the Register of Deeds office
- Inspecting the property from the street
- Checking your list to ensure you have everything you need

A large part of foreclosure *invest*ing consists of *invest*igating — knowing what you're about to buy before you lay your cash on the line. You need to know how much the property is worth, how much is owed on it, whether it has any additional liens or encumbrances on it, whether the property is in violation of any building codes, and whether the person selling the house is really the legal owner.

TIP

For each property you consider buying, create a separate folder with a photo of the property, its address, and all publicly accessible information available for that property. This chapter shows you the type of information you need and provides instructions on how to dig it up and gather it into a file to create your very own custom property dossier.

In addition to assisting you in determining whether the property is worth your time pursuing, this information becomes critical in assisting homeowners, negotiating with homeowners and lenders, and bidding on a property at auction.

Collecting Essential Information about the Property

Every property has some vital statistics that must find their way into your property dossier. You can collect most of the data you need through the Notice of Default (NOD) or foreclosure notice (if one has been posted) and from your county's courthouse and city or town offices. Chapters 7 and 9 point you in the direction of foreclosure notices. Later in this chapter, I show you how to pick essential details off of the foreclosure notice and dig up additional information at the county courthouse.

If you're working with the homeowners prior to the start of foreclosure proceedings, gather as much information as you can from the homeowners first, as explained in Chapter 9. You need to know as much as possible about their situation in order to be of assistance and minimize your own risk as an investor.

In the following sections, I point you to the sources of key information and provide a couple forms to complete to record the essential data in a format you can quickly reference later.

Honing your title acquisition and reading skills

TIP

To hone your skills at gathering data related to foreclosure properties, consider practicing on your own home first. Of course, unless you're currently in foreclosure, you won't have access to a foreclosure notice (lucky you), but you can practice researching your title, mortgage, and other documentation relating to your property. You may have several of the documents you need to practice on in the closing packet you received when you purchased your home, but don't cheat by referring to those documents. Go out in the field and see what sorts of publicly accessible data you can gather on your own:

1. **Head down to your local title company.** You can find a list of title companies in your phone book.
2. **Meet with one of the representatives and explain that you're reading this book called *Foreclosure Investing For Dummies,* and you want to know everything they can teach you about titles.**

Getting burned by bad decisions

Dr. Beecher, highly educated and very successful in her field, attended a seminar on foreclosure investing. She purchased the books and CDs for sale at the seminar, studied them carefully, and decided to begin purchasing foreclosure properties.

The system seemed straightforward enough, so she began attending auctions and purchasing properties right out of the shoot. Well, she *thought* she was purchasing properties. At foreclosure auctions, you actually purchase foreclosed-upon mortgages. If you buy a first mortgage, you're likely to take possession of the property after the redemption period. Second mortgages and other liens against the property are usually wiped out by the foreclosure process — in most cases, they're worthless.

The doctor bought about seven or eight second mortgages, thinking that she would be owning the properties when the redemption periods expired.

Paul, my buyer at foreclosure auctions, observed the doctor over the course of a couple weeks. One week, Paul approached her and asked if she understood what she was doing. During the conversation, Paul realized that the doctor was following some bad advice. He brought her back to the office to meet me.

We researched the properties for her and helped her understand what she had actually done. She had purchased several second mortgages that were destined to become worthless pieces of paper — the foreclosure would wipe them off the books. She invested about $100,000 and was going to lose all of it. That was a tough lesson to learn, but with her newfound understanding, the doctor went on to become a successful real estate investor.

The moral of the story is to do your homework before you start investing. Know what you're buying, before you put your money on the line.

3. **Request a title commitment on your own property.** They may take a couple days to prepare the title commitment. Offer to pick it up when it's ready, so they won't have to pay postage.
4. **Visit your county courthouse and track down the Register of Deeds.**
5. **Ask nicely to see everything recorded against your house in the last 24 months.** In some cases, the records may not go that far back, but you should be able to obtain the last two recorded documents — perhaps the deed and the mortgage showing when you purchased the property.
6. **Now, compare the title commitment you received from the title company with the documents you picked up with your own detective work.**

You should notice a big difference in the documents. The title commitment won't include all the information from the documents you picked up at the county courthouse. Instead, it extracts the essential details and presents them in a more easily accessible format, showing:

- Homeowners' names
- First mortgage
- Any second mortgage or other liens against the property
- Property taxes paid or due
- Delinquent water bills or other services supplied by the municipality

Picking details off the foreclosure notice

When a NOD or foreclosure notice is published, like the one shown in Figure 8-1, you have a wealth of information at your fingertips. The NOD or foreclosure notice presents you with the following details that you can record on foreclosure information sheet, shown in Figure 8-2:

- **Case or reference number[1]:** Some attorneys include a case or reference number in the foreclosure notice to simplify the process of searching for information in their database.
- **Insertion date[2]:** The date may appear in the notice itself, but if it doesn't, use the date of the publication in which the notice is posted. In the legal news, the advertisements are listed under subtitles to indicate the order of the posting — first, second, third, and so on.
- **County[3]:** The county in which the property is located is your key to unlocking other details about the property. Using this bit of information, you know which county's register of deeds office to visit to research the title and mortgage and find the property's address. (Start off working in the county where you live.) This may not be an issue if the paper you are using is county specific, in which case, pay attention to the city and focus on the city where you live or the cities that are most familiar.
- **Legal lot, subdivision, and city[4]:** The legal description of the property does not provide the property's mailing address, but from the legal description, you can find the mailing address. See the later section, "Finding the property," for details.
- **Name of the mortgagor[5]:** The mortgagor is the borrower, typically the homeowners — the person or people who owe the money, even if they're not in possession of the property.

- **Name of the mortgagee[6]:** The mortgagee is the lender who is foreclosing on the property.
- **Amount owed on the mortgage[7]:** The NOD or foreclosure notice always states the exact amount the homeowners currently owe on this mortgage. They may owe additional sums on other loans. The amount owed changes between the time the notice is published and the sale occurs, so call the foreclosing attorney closer to the date of sale to determine the actual opening bid amount.
- **Interest rate of loan[8]:** The longer the amount owed on the mortgage remains unpaid, the amount increases by the specified interest rate. This can help you track the amount owed as it increases over time. In addition, this is the interest rate you earn if you purchase the mortgage and someone purchases it back from you during the redemption period.
- **The mortgage company's attorney[9]:** The mortgage company attorney's name and contact information is useful in enabling you to double-check the sale date and the opening bid and contact the mortgage company to work out a deal.
- **Mortgage sale date[10]:** This is the date on which the attorney for the lender expects the mortgage to be auctioned. This date can change, but jot it down, so you can keep track of it.
- **Length of the property's redemption period, if applicable[11]:** If your area has a mandatory redemption period, it should appear in the NOD or foreclosure notice. Using the date of sale and redemption period, you can determine the last day the homeowners can redeem the property. Verify the redemption period with your own research; occasionally the wrong redemption period is published.
- **Liber (the legal book in which the deed is recorded at the county courthouse) and page number of the recorded mortgage that is in foreclosure[12]:** This tells you where to find the mortgage document and which mortgage is being foreclosed on if the homeowners have more than one mortgage on the property.

If you're buying properties directly from homeowners who contacted you prior to the beginning of foreclosure proceedings, you can gather most of the information you need to complete the foreclosure information sheet from the homeowners, as explained in Chapter 9. Just be sure to verify the information by inspecting the title and other records as explained in the following sections.

ROBERTS & KRAYNAK, P.C.
Attorneys and Counselors
1313 Mockingbird Ln., Ste. 200
Dellingham Farms, MI 48025

THIS FIRM IS A DEBT COLLECTOR ATTEMPTING TO COLLECT A DEBT. ANY INFORMATION WE OBTAIN WILL BE USED FOR THAT PURPOSE. PLEASE CONTACT OUR OFFICE AT THE NUMBER BELOW IF YOU ARE IN ACTIVE MILITARY DUTY.

ATTN PURCHASERS: This sale may be rescinded by the foreclosing mortgagee. In that event, your damages, if any, shall be limited solely to the return of the bid amount tendered at sale, plus interest.

MORTGAGE SALE - Default has been made in the conditions of a mortgage made by JOHN Q PUBLIC and JANE Q PUBLIC[5], husband and wife, original mortgagor(s), to Federal City Mortgage Co D/B/A Commonwealth United Mortgage Company[6], Mortgagee, dated March 4, 2002, and recorded on April 10, 2002 in Liber 55555 on Page 617[12], in Oakland county[3] records, Michigan, on which mortgage there is claimed to be due at the date hereof the sum of Four Hundred Seventy-Two Thousand Seven Hundred Fifty-Eight And 23/100 Dollars ($472,758.23)[7], including interest at 5.625% per annum[8].

Under the power of sale contained in said mortgage and the statute in such case made and provided, notice is hereby given that said mortgage will be foreclosed by a sale of the mortgaged premises, or some part of them, at public venue, at the Main entrance to the Court House in Pontiac at 10:00 AM, on **JANUARY 31, 2007**[10].

Said premises are situated in Charter Township of West Bloomfield, Oakland County, Michigan, and are described as:

Homesite No. 55, Amberleigh Condominium, according to the Master Deed recorded in Liber 55555, Pages 665 through 730, Oakland County Records, as amended, and designated as Oakland County Subdivision Plan No. 1555[4] together with rights in the general common elements and the limited common elements as shown on the Master Deed and as described in Act 59 of the Public Acts of 1978, as amended

The redemption period shall be 6 months from the date of such sale[11], unless determined abandoned in accordance with MCLA 600.3241a, in which case the redemption period shall be 30 days from the date of such sale.

Dated: December 30, 2006[2]
For more information, please call:
FC F 555.555.5555
Roberts & Kraynak, P.C.[9]
Attorneys For Servicer
1313 Mockingbird Ln., Ste. 200
Dellingham Farms, MI 48025
File #055000F05[1]

Figure 8-1: Collect important details about the foreclosure property from the Notice Of Default (NOD).

Foreclosure Information Sheet

Date: ______________

Foreclosure Notice

Case or Reference Number: ______________________________

Insertion Date: ______________ Thru:

County: ______________________________

Legal Lot: ______________________________

Subdivision: ______________________________

City: ______________________________

Mortgagor (Homeowners): ______________________________

Mortgagee (Lender): ______________________________

Mortgage Amount: ______________________________

Interest Rate: ______________________________

Mortgage Company's Attorney: ______________________________

Mortgage Company's Attorney Phone Number: ______________________________

Mortgage Sale Date: ______________________________

Redemption Period: ______________________________

Last Day to Redeem: ______________________________

Register of Deeds (Title)

Property Address (Ask Clerk): ______________________________

Mortgagor Names: ______________________________

Price Paid for Property: ______________________________

Deed Warranty Names: ______________________________

Previous Mortgagor (Previous Title): ______________________________

Price Paid for Property (Previous Title): ______________________________

Current 1st Mortgage Mortgagee (Lender): ______________________________

Original Mortgagee (Lender): ______________________________

Register of Deeds (1st Mortgage and Note)

1st Mortgage Loan Amount: ______________________________

Interest Rate: ______________________________

Date Recorded: ______________ Liber: ________ Page: ______________________________

Mortgagee (Lender): ______________________________

Address: ______________________________

Figure 8-2: Record information from the foreclosure notice and public records on the foreclosure information sheet.

Mortgage Assumable? ☐ Yes ☐ No

Register of Deeds (Second Mortgage and Note)

2nd Mortgage Loan Amount: ____________________

Interest Rate: ____________________

Date Recorded: __________ Liber: ______ Page: ____________________

Mortgagee (Lender): ____________________

Address: ____________________

Mortgage Assumable? ☐ Yes ☐ No

Register of Deeds (Additional Mortgages or Liens)

Junior Lien Holder 1: ____________________

Address: ____________________

Junior Lien Holder 2: ____________________

Address: ____________________

Tax Lien: ____________________

Address: ____________________

County Tax Assessor

Sidwell (Tax ID #): ____________________

Taxable Value (SEV): ____________________

Property Tax Formula: ____________________

Unpaid Property Taxes: ____________________

Property Tax Lien? ☐ Yes, Amount: ______________ ☐ No

State, County, City or Town Property Worksheet

Building Permits: ____________________

Code Violations: ____________________

Other: ____________________

Other Information

Opening Bid: ____________________

Homeowner's Phone: ____________________

Estimated Property Value: ____________________

Total Owed on Property: ____________________

Estimated Equity in Property: ____________________

The chicken man

One of the most successful foreclosure investors in our area has been dubbed "The Chicken Man," because he delivers buckets of chicken to the staff members in the register of deeds office. By catering in lunch on a regular basis, The Chicken Man has established an outstanding relationship with the clerks. He can literally walk in through the back door of the register of deeds office and help himself to the records. When he can't find a record he needs, the clerks are more than willing to lend a hand. You might say that The Chicken Man has a leg up (and a wing and a thigh and a breast) on the competition.

Before you step into the register of deeds or county clerk's office, turn on your charm and brush up on your manners. Ask politely for assistance and say "thank you" when the people behind the desk provide that assistance. The office staff stands between you and the information you need, and they are usually as helpful as you are polite.

Digging up details at the register of deeds office

Whether you're planning to bid on a property at auction or purchase the property directly from homeowners, a trip to your county's register of deeds office is a necessity. The register of deeds or county clerk is the one who records most of the legal paperwork for a property, including the title work, deed, and mortgage. In the following sections, I point out the essential information you need to scrounge up from this most important source.

The records you need to research can be recorded on any of several types of media. You may be pulling out folders, flipping through pages in a book, or looking for records on microfilm.

Finding the property

The NOD or foreclosure notice describes the location of the property through a legal description rather than simply providing a mailing address. Isn't that just like lawyers? Fortunately, you can use the property description to track down the mailing address, by employing one of the following strategies:

- Ask the clerk at your county's register of deeds office.
- Ask your real estate attorney.

- Contact your title company. If you have a good relationship with the company, they may be willing to look up the address for you.
- Use a land data software program to search a database of property information. Land data software programs are available in some areas and on the Web.

TIP

Some companies, such as HomeInfoMax at www.homeinfomax.com, provide online search tools that can assist you in finding a property's address based on its legal description. However, most online tools don't cover all counties and typically charge per search. You can get the information for free by doing a little legwork or dialing the phone.

Once you have the address, plug it into an online mapping program you use and print a map of the property's location. I also use Google Earth to print a satellite image of the property. Keep in mind, however, that satellite images are often months or even years old — they're no substitute to actually driving to the property and inspecting it with your own two eyes. See "Doing Your Fieldwork: Inspecting the Property," later in this chapter.

Obtaining the property's title and other key documents

When most homeowners buy a property, they agree to buy the property from the seller before any mention of the title. Prior to closing on the transaction, they hire a title company that inspects and insures the title to protect the buyer from any messy legal battles over who owns the property.

When buying foreclosure properties, however, inspect the title before you decide to pursue a property. If anything about the title smells fishy, then you may want to do a little extra research or simply cross the property off your list.

You can do your preliminary title research yourself by heading down to your county's register of deeds office and asking the clerk to provide you with the information of what is recorded on title for a particular property. At the bare minimum, obtain a copy of the deed and any other recorded documents for the current and previous owner. If possible, obtain copies of all documents recorded in the past 24 months.

TIP

Although you can do this research yourself, and you really should do it yourself to learn about title research, I recommend that when you're first starting out, you consult your title company for a second opinion and order a title commitment. Once you feel comfortable doing your own research, you can take on more of the burden. For more about title commitments, see Chapter 4.

Researching the property's title

Inspect the title work and deed for the following critical pieces of data and record them in the corresponding spaces on the foreclosure information sheet, shown in Figure 8-2:

- **Mortgagor (homeowners') names:** Note whether the mortgagor's name matches the name actually listed as the property's title holder. Differing names raise a red flag — make a note of it.
- **Price paid for the property:** Depending on how long ago the current homeowners purchased the property, this can provide some indication of the property's current value.
- **Deed warranty names:** The names on the deed should match the homeowners' names on the title. If they don't match, the difference raises a red flag — make a note of it.
- **Previous mortgagor:** Check the previous title and jot down the names on the title. Note any chinks in the chain of ownership. If the title work shows that Johnson sold the property to Davis and then Howard sold it to Pinkerton, who did Davis sell the house to? This gap would indicate a problem in the chain of ownership. Consult with your title company whenever you notice any irregularities in the chain of title. Take note of maiden-name changes — changes in names after divorce — a name change may result in what only appears to be a gap in the chain of ownership.
- **Previous price paid for the property:** This isn't a crucial piece of data, but it can point to a pattern of an increasing or decreasing property value.
- **Current first mortgage mortgagee (lender):** The first mortgage mortgagee is the bank or other lending institution that holds the first (senior) lien on the property. By obtaining the lender's name from the title, you can begin the process of tracking down the lender. Their information should be on the actual mortgage document, a copy of which you can obtain at the Register of Deeds office. For more about liens, including which liens take precedent, see "Uncovering facts about additional lender liens," later in this chapter and check out Chapter 15.
- **Original first mortgage mortgagee (lender):** In many cases, a lending institution loans the homeowners money to buy the property and then sells the mortgage almost immediately to another lending institution. The title typically includes the name of the original lender. When you start making calls, having this information at your fingertips helps convince the person you contact that you know what you're talking about.

Protecting yourself against mortgage fraud

By carefully researching the properties that interest you, particularly the legal documents associated with them, you protect yourself not only from inadvertent errors but also from con artists who are trying to fleece you. Con artists often manipulate the legal documents and file false documents as part of their scams. Sometimes, they can even sell a house they don't own or sell a house several times to different buyers. To protect yourself from falling victim to a real estate scam, take the following precautions:

- Check the records to see if the mortgage on the property was recently paid off. Sellers rarely pay off mortgages right before they sell, so any document that shows the mortgage as having been recently paid off is likely to be a phony document.
- Be wary of an investor who's pitching you a great deal on a property. Con artists often target novice investors in double-sales scams.
- Analyze the title commitment for suspicious transactions.
- Ask your title company for a 24-month property history, including mortgages.
- Purchase title insurance as soon as possible and pay for it up front. Sometimes, this is your only protection.

If the property has a second mortgage on it, record the same information for the second mortgage. You may be able to work with the second mortgage lender to shore up your position. See Chapter 9 for additional details on collaborating with lenders.

Gathering information from the mortgage and note

The mortgage and note are also recorded along with the title when someone purchases a property. These documents include important details about the senior lien, so be sure to record these details on your foreclosure information sheet:

- **First mortgage loan amount:** How much did the homeowners borrow to finance the purchase of the property?
- **Interest rate:** Knowing the interest rate on the first mortgage can assist you in calculating the homeowners' current monthly payments and providing them with refinance options.
- **Date recorded, liber, and page number:** With the date recorded, liber, and page number, you can access the information much more quickly.
- **Mortgagee (lender):** You may have already obtained the mortgagee's name from the title, but check the mortgage for any discrepancies. Also, jot down the mortgagee's address for future reference.

Uncovering facts about additional lender liens

Although the first (senior) lien is the most important, the property may have other liens from second or third mortgages or construction liens that you should know about. Unless the homeowners very recently took out another loan using the property as collateral or the register of deeds is way behind in recording documents, records of these liens should be accessible.

Some liens take precedence over others. Buying liens with a higher precedence gives you more power. Property tax liens almost always take precedence over other liens. Then, the pecking order usually follows the dates on which the loans agreements were executed and recorded. This typically gives the first mortgage the most power. If you order a title commitment, it lists the liens in order of precedent. If you do your own research, you have to do this yourself. For more about the lien pecking order, see Chapter 15.

On your foreclosure information sheet, record the names and addresses of any additional lien holders. The date on which a lien was recorded should alert you to the fact that a particular lien is a junior lien. The liber and page number on which the junior lien was recorded should also be higher than that of the senior lien, because the junior lien was recorded later.

Uncovering unpaid property taxes and other tax liens

When homeowners get behind on their taxes, government agencies at the federal, state, or county level can place additional liens on the property. While researching the title, inspect it for any of the following additional liens:

- IRS federal income tax liens.
- State income tax liens.
- Property tax liens.
- Any other liens.
- Record of deceased owner (if the death certificate is on the title). If you see a death certificate and the property is in foreclosure, try to locate the probate attorney whose in charge of liquidating the property. To locate the attorney, head down to the county building, visit the probate office, and ask whether anyone has opened a probate case in the name of the deceased party. If the case is in probate, ask to see the file, which will contain the name and contact information for the person handling the case.

Additional liens, most importantly liens for overdue property taxes and IRS tax liens, are a good sign that the homeowners will be unable to redeem the property. They're probably too deeply in debt to catch up on their payments.

Gathering tax information at the assessor's office

In addition to checking the title for any property tax liens, head down to the county treasurer's or assessor's office and ask for the following:

- The property's tax ID number (often called a *property identification number* or PIN) — the number that the city or county taxing authority assigns to the property for reference and tracking. Some cities (Detroit, for example) have ward numbers that serve the same function. Regardless of what the number is called, it identifies a specific parcel of land. Once you get a feel for the identification system, you can almost tell just by the number where the property is located.
- The taxable value of the property — you may have to visit the county assessor's office for this tidbit. Knowing the taxable value of a property may assist you in guesstimating the property's market value, but it is no substitute for an accurate current appraisal or your own research on market values of comparable properties. In some cases, the taxable value may be expressed as SEV (state equalized value). SEV may represent a fraction of the actual assessed value of the property; in some areas, for example, the SEV is calculated as half of the previous sales price.
- The property tax formula. Currently in Michigan, a house is generally worth 2 to 2.2 times the SEV, so a house with an SEV of $200,000 is worth $400,000–$440,000. Ask the assessor what formula he uses. This can often provide you with a rough estimate of the property's market value.
- Whether property taxes are currently paid up and whether the assessor's office has a property tax lien on the property.

Getting your hands on the property worksheet

Every town, city, or county in the United States keeps a worksheet on every property showing when it was built, any building permits issued on the property, code violations, inspection reports, and so on. Find out who keeps the property worksheets and obtain a copy of the worksheet for any home you are considering buying. On your foreclosure information sheet, record the following data from the property worksheet:

- **Building permits:** Building permits provide a record of all approved property improvements. If you inspect the property later and discover an improvement that was performed without a permit, this may be a warning that the improvement does not conform to building codes.

- **Code violations:** If the property has any code violations recorded against it that have not been resolved, you want to know about it, so you don't unknowingly take possession of a property that you're responsible for bringing up to code later.
- **Other interesting tidbits:** The property worksheet may include additional information about health code violations that warn you to inspect the property more closely before purchasing it. For tips on physically inspecting a foreclosure property, see "Doing Your Fieldwork: Inspecting the Property," later in this chapter.

WARNING!

A permit showing that the work passed final inspection is best. That shows that no matter who pulled (obtained) the permit (the homeowner or a licensed contractor), the work was completed and was at least up to code. Open permits — those that don't indicate that the work passed final inspection — may indicate that the work was completed to code or that you're going to be in for some costly repairs. In any event, knowing what's been recorded with the city concerning work begun or completed on the property is beneficial.

Gathering additional information

To complete the foreclosure information sheet, do a little extra detective work to gather the following additional details:

- **Opening bid:** If you found out about the property through a NOD or foreclosure notice, call the attorney listed in the notice to find out the opening bid.
- **Homeowner's telephone number:** Finding the homeowners' phone number can be challenging, especially if their phone's been disconnected or the number is unlisted. Using the homeowner's name and the property address, try looking up the phone number online at a site such as `www.whitepages.com`. If you can't get the phone number, don't worry. In Chapter 9, I provide some additional tips for finding homeowners.
- **Estimated property value:** The property's current value is how much the homeowners could get for the property if they sold it today. You can obtain a ballpark estimate by checking the prices of comparable homes that have sold in the past month or so. A real estate agent can come in handy here. Refer to Chapter 10 for details.
- **Total owed on the property:** Add up the balance on all liens against the property. You can come up with a pretty accurate figure by adding up the original balances and deducting estimated payments. If the loans are less than 10 years old, chances are pretty good that the balances haven't been paid down very much, because a good chunk of each payment in the early years is applied to interest, not principal.

Doing Your Fieldwork: Inspecting the Property

An investment property may seem like a steal on paper when it's actually a gutted shell of a home in the center of the low-rent district. Until you see the property for yourself, you have no idea what it is, what kind of homes surround it, or what condition the home is in.

Before you plop down your money or borrowed money on a property, always inspect it as closely as possible with your own two eyes, carefully record your observations, and add the details you gather to your growing property dossier. In the following sections, I provide an exterior home inspection form to complete, and I lead you through the process of performing your due diligence in the field.

Doing a drive-by, walk-around inspection

The least you should do (and the most you can do in some situations) to inspect a property is to drive over and walk around the property — at a safe distance, of course — I'm not suggesting that you trespass. Even if you can't get inside to take a closer peek, the drive-by, walk-around inspection provides you with enough preliminary information to develop a ballpark estimate of the property's value and rule out any really bad properties.

Whenever you visit a property in person, you're at some risk. The homeowners, and sometimes their dog, may not appreciate uninvited visitors, especially if you trespass. Keep your distance. Knocking on the front door is usually okay, but if the homeowners ask you to leave, respect their wishes and follow up with a letter, as explained in Chapter 9.

As you perform your drive-by, walk-around inspection, complete the exterior inspection form provided in Figure 8-3. (I don't write very neatly, so I take along a digital recorder, record my observations, and then burn the audio clip to a CD to add to my file.) You may be unable to collect all of the information requested on the form, but collect as much information as possible without becoming too pushy if the homeowners confront you.

If the home is currently listed for sale, call the agent and take a tour of the inside of the house. You don't need to tell the agent that you know the homeowners are facing foreclosure. In Chapter 9, I provide an inspection form for the interior of the property — take the form with you and fill it out.

Exterior Property Evaluation

Owner: ______________________________

Home Phone: __________ Work Phone: __________ Pager/Mobile: __________

Address: ______________________________

Distinguishing Feature of Property: ______________________

Property is: ❑ Vacant ❑ Owner Occupied ❑ Tenant Occupied

Tenant Info: How Long at Home? ______ Monthly Rent: __________

Neighborhood Details: ❑ Brick ❑ Frame ❑ Mix

Block Club? ❑ Yes ❑ No

# of burn-outs: ____ #of board-ups: _____ #of vacant lots: _____ %ownership: _________

Neighborhood Rating: ❑ Poor ❑ Fair ❑ Good ❑ Excellent

Neighborhood Listings:

Address: ______________ Phone: ________ Asking Price: __________

Address: ______________ Phone: ________ Asking Price: __________

Address: ______________ Phone: ________ Asking Price: __________

House Details:

Garage: ❑ Yes ❑ No # of Cars: ____ Condition: ❑ Poor ❑ Fair ❑ Good

Driveway: ❑ None ❑ Solid ❑ Ribbon ❑ Asphalt ❑ Alley

Condition: ❑ Poor ❑ Fair ❑ Good

Roof Type: ________ Age: ________ Condition: ❑ Poor ❑ Fair ❑ Good

Type of Construction: ❑ Brick ❑ Frame ❑ Aluminum ❑ Block

❑ Asbestos ❑ Vinyl ❑ Brickote ❑ Stucco

Condition: ❑ Poor ❑ Fair ❑ Good

Year Built: ________ Square Footage: __________ Number of Bedrooms: ___

House Style: ❑ Tudor ❑ Bungalow ❑ Ranch ❑ Split-Level

❑ Colonial ❑ Cape Cod ❑ Multi-Family: __________

Foundation: ❑ Basement ❑ Slab ❑ Crawl ❑ Piers

Storm Doors/Storm Windows/Screens Condition: ❑ Poor ❑ Fair ❑ Good

Window Condition: ❑ Poor ❑ Fair ❑ Good Lot Size: _________

Fence: ❑ Chain ❑ Wood ❑ Wire Landscape: ❑ Poor ❑ Fair ❑ Good

Porch: ❑ Cement ❑ Wood ❑ Brick Condition: ❑ Poor ❑ Fair ❑ Good

Steps: ❑ Cement ❑ Wood ❑ Brick Condition: ❑ Poor ❑ Fair ❑ Good

Door: ❑ Wood ❑ Steel Condition: ❑ Poor ❑ Fair ❑ Good

Recommendation: ❑ Cash Buy ❑ Re-Fi ❑ Listing ❑ Short Sale ❑ Pass

❑ Other: ______________________________

Reasoning/Notes: ______________________________

____

____

Figure 8-3: Personally inspect the neighborhood and the exterior of the property and record your observations.

TIP

Never pass up the opportunity to talk to a neighbor. If a neighbor wanders out to ask what you're doing, strike up a conversation and try to find out more about the homeowners and the condition of the property. No nosy neighbors? Then consider becoming a little nosy yourself and knocking on doors. A neighbor may have recently been inside the house. If you can't get in to inspect the property, a second-hand report from a neighbor is the next best thing. In some cases, you may even stumble across a neighbor whom the homeowner has anointed to be caretaker; if she has keys and is willing to show you around, you've struck gold! For tips on how to do an interior inspection and an interior inspection form skip, to Chapter 9.

Snapping some photos

Every real estate investor should own a high-quality digital camera with a 3x or better zoom lens to take snapshots of prospective investment properties. As you walk around the property, take a couple photos of every side of the house, the landscape, and surrounding houses. The photo documentary you create is priceless. If you inspect dozens of properties, you're not likely to remember a specific house. A few photos can bring you right back to the day when you first inspected the property.

If possible, take your photos late morning or early afternoon, when the homeowners are more likely to be at work and the kids in school, to avoid any confrontation with the homeowners and keep the kids from asking their parents embarrassing questions like, "Why is that lady taking pictures of our house?" You can also keep a low profile by snapping photos from inside your car. Whatever you do, just make sure you're on public property — the sidewalk or street, rather than in someone's yard.

In addition to photographing the property itself, photograph the neighborhood:

- Take a photo of the street view both ways.
- Take a picture of the houses across the street.
- Photograph any eyesores.

If your camera has a time stamp feature that places the day's date and time on every photo, turn on the time stamp, so you can coordinate your photos with your property data sheets. If you take photos of several properties in the course of a week and wait a few days before printing your photos, you may not recall which house the photos represent.

As soon as possible after snapping the photos, print them or take them to your local photo shop to have them processed. Stick the photos in your property dossier for later reference. Burn them onto a disc and save them with the file to avoid cost.

Assembling Your Dossier: A Checklist

For every property I investigate, I create a separate folder for all the documents pertaining to that property. I use different-colored folders to keep data for my top prospects separate. I recommend a similar strategy, but you feel free to be creative — just make sure your system keeps all the data on each house separate and easily accessible. You can even store the information in separate folders on a portable computer.

However you choose to organize your property information, make sure each folder contains the following items:

- 8-by-10-inch photograph of the property taped to the front of the folder for quick reference.
- The foreclosure notice.
- The foreclosure information sheet you completed.
- The exterior inspection form you completed.
- Neighborhood inspection, complete with photos.
- Information on any other properties that are listed for sale in the area, so you can track the sales price and how long it took to sell.
- A map showing the location of the property.
- The title commitment and 24-month history in the chain of title or the minimum last two recorded documents.
- The last recorded first mortgage, so you know how much the homeowners currently owe on the property.
- Records of other liens on the property, such as second mortgages, construction liens, and tax liens. Property tax liens are especially important, because if you buy the property, you're responsible for paying any back property taxes.
- A copy of the deed with the current homeowners' names. These names should match the names on the title.
- The city worksheet on the property showing the history of the property.
- The SEV (state equalized value).
- MLS listings of comparable properties that have recently sold or are currently for sale.

If you gathered information to bid for properties at an auction, pack all of your folders with you. You may have researched 20 properties and narrowed down your prospects to the top 3, but take all 20 folders with you, because you never know what will happen come auction day. You may have ruled out a $250,000 house that had a $260,000 mortgage on it, but then, when the auction rolls around, it may open with a bid for $170,000. By quickly referencing your property dossier and doing some basic math, you realize that you can pick up $80,000 in equity. Because you've done your homework and you have your file with you, you may be the only one in the room who knows what that house is worth. When that happens, you're like a fox in the henhouse.

Chapter 9

Contacting the Homeowners and Lenders

In This Chapter

- Drawing up a foreclosure activity schedule
- Establishing a solid relationship with distressed homeowners
- Gathering key information from the homeowners
- Explaining the homeowners' options
- Inspecting the property's interior
- Negotiating deals with lenders

When you choose to deal directly with homeowners facing foreclosure, you become the resident rescue worker in a burning building. Your job is to assess the situation, point out the exits, and do everything in your power to assist the homeowners in extinguishing the flames or safely retreating from the building.

As a foreclosure rescue worker, you must first contact the homeowners and obtain detailed information about their situation. This requires an empathetic ear and the ability to jot down the most important details. With this information and the details about the property (see Chapter 7), you can then assess the situation and lay the homeowners' options on the table. Perform your job well, and you earn the homeowners' trust and place yourself in a better position to obtain the property should they choose to sell it.

In this chapter, I lead you through the process of contacting the homeowners, gathering information about their situation, and presenting their options to them. I also show you how to deal effectively with lenders to negotiate a solution that's less painful for all involved.

Scheduling Your Foreclosure Activities

Having a game plan for researching the property and contacting the homeowners and lenders is always a good idea. By planning your activities in advance, you create a schedule that keeps you on track and in touch with the homeowners and lenders.

Your schedule is generally dictated by the time span between the posting of the foreclosure notice and the sale and on the redemption period, if you have a redemption period in your area. If your area has a redemption period, you can continue to educate and work with the homeowners even after their home has been sold at auction.

REMEMBER

Planning is important, but be flexible. The foreclosure process is predictable, but the homeowners and their situation are often very unpredictable. Be prepared to ride some serious waves.

In Michigan, the foreclosure notice is published four-to-six consecutive weeks before the sale and is typically subject to a redemption period of six months or more. My plan kicks into action as soon as I spot an interesting foreclosure notice and continues for four consecutive weeks. Start with the following plan and tweak it to conform to the foreclosure schedule in your area:

Week 1:

1. **Find the foreclosure notice or NOD (Notice of Default).**
2. **Do some preliminary research on the property, as explained in Chapter 7:**
    - Find the property's address.
    - Visit the property to see if it's something you'd be interested in purchasing.
    - Take photos of the property, if you're interested.

   REMEMBER

   Don't waste time or resources ordering a title commitment or heavily researching a property that you have no intention of buying. At this point, you're just trying to spot the best prospects. Once you have a short list, you can do more research.
3. **Send your first foreclosure letter introducing yourself to the homeowners.** See "Delivering a letter of introduction," later in this chapter.

Week 2:

1. **Find second foreclosure notice.**
2. **If the notice does not appear, send a congratulations letter to the homeowners.**

3. **Review the title work.**
4. **Attempt to contact the homeowners by phone.**
5. **Knock on door to attempt face-to-face meeting.**
6. **Send your second foreclosure letter.**

Week 3:

1. **Find the third foreclosure notice.**
2. **If a third notice does not appear, send a congratulations letter to the homeowners.**
3. **Attempt to contact the homeowners by phone.**
4. **Research the property more thoroughly if it appears to be a hot prospect:**
   - Research comparable sales.
   - Order a title commitment or obtain the title work yourself.
5. **Contact the junior lien-holders.** See "Contacting the Lenders," later in this chapter.
6. **Contact mortgagee's attorney, and find out if:**
   - The property is still going to auction.
   - If there is an opening bid and what the opening bid amount is.
   - If they are considering an adjournment (postponing the sale), which is usually a sign that the homeowners and lender are negotiating a possible solution.
   - Any other background information. Feel them out for a possible short sale. Chapter 15 provides additional information about negotiating short sales.
6. **Send your third foreclosure letter.**

Week 4:

1. **Find fourth (probably final) foreclosure notice.**
2. **If a fourth notice does not appear, send a congratulations letter to the homeowners.**
3. **Drive by the house you are interested in bidding on at auction and take new photos if the condition of property has changed significantly.**
4. **Attempt to contact the homeowners by phone.**
5. **Send your fourth foreclosure letter.**
6. **Organize your property dossier for the auction.**

Avoiding legal brouhahas: Ignorance is no excuse

Prior to contacting the homeowners directly, brush up on the legal and ethical rules of the foreclosure game, so you don't get slapped with a lawsuit and you can look yourself in the mirror every morning and know that you're not ripping off distressed homeowners. Here are the do's and don'ts you must follow to work foreclosures ethically and legally:

- Never do anything to mislead homeowners into thinking you're something you're not, such as an attorney, accountant, or financial advisor. Let homeowners know up front that you are an investor who purchases properties. If you are a real estate agent, you must disclose the fact that you act in both capacities.
- Always let the homeowners decide what is best for them. You can present their options, but this is their home and their debt. Don't steer them into selling the property to you simply because it's in *your* best interest.
- Always recommend that the homeowners contact their lenders directly or consult an attorney or accountant if that would be in their best interest. If they are hesitate or afraid to call their lender, you can have them sign an authorization form and call the lender with them. Unfortunately con-artists use an authorization form to collect personal information that enables them to rip off distressed homeowners.
- Present all of the homeowners' options to them, including the option to file for bankruptcy, even if that means that you lose out on the deal.
- Don't befriend the homeowners' for the sole purpose of convincing them to hand the house over to you.
- If you decide to purchase the property from the homeowner, put your offer in writing on a purchase agreement. In real estate, only agreements in writing stand up in court.
- Avoid any contact with the homeowners during the last month of the redemption period. At this point, homeowners may become very desperate and accuse you of making promises you never made. The unfortunate reality is that this is exactly when they will contact you, usually from one of the letters you sent that they have been holding on to. If you do talk with them, record the conversations as protection, provided that you have the legal right to record conversations.
- Audiotape your conversations with homeowners, whether you meet with them in person or talk on the phone. Bring a recorder and ask permission to record the conversation for their protection and yours. This way no one can conveniently forget what was actually said.

Anyone with a bad attitude and a hundred bucks can file a lawsuit. My company was dealing with a couple who were facing foreclosure. The wife never told the husband that she had not made the payments until they lost the house. We told her that she needed to come to the office to find out more about their options. The last week of the redemption period was the beginning of hunting season, and the husband was out of town, so they never showed up for the scheduled meeting. They retained an attorney who sued us. Their claim was that we had promised they could stay in the home. They lost the case and then hired another attorney.

I strongly encourage you to consult a real estate attorney familiar with foreclosure laws in your market before working foreclosures in your area. Also, find out about your legal rights for taping conversations. In Michigan, you can legally tape a phone conversation as long as you're in on the conversation.

If your state has no redemption period, stress to the homeowners that they are very likely to lose their house and all of its equity unless they take action *before* the mortgage sale. In areas with redemption periods, homeowners still have time after the sale to take action, but the longer they wait, the less attractive are their options.

If your area uses NODs, begin by contacting bank REO Departments as soon as the NOD is filed. See Chapter 12 for details.

I track foreclosures using a computer program called ACT. For each property, I add the homeowners as contacts and add reminders for each week telling me just what to do and when to do it. With reminders set for specific dates, whenever I run ACT, the program notifies me when I need to call, write, or visit a prospective client. Use whatever software or system works for you, but be sure you have an effective system in place.

Contacting the Homeowners Directly

To purchase properties directly from homeowners prior to auction, you have two big challenges ahead of you: tracking down the homeowners and getting them to sit down with you at the kitchen table to discuss their situation. Rarely do homeowners who are facing foreclosure seek help. Most often, in an attempt to avoid the situation, they do everything they can to avoid lenders, collectors, attorneys, and investors . . . yeah, people like you.

In the following sections, I reveal strategies and tips that I use to track down homeowners and make a good first impression when I contact them.

Many real estate investors avoid foreclosures, because the homeowners can be so difficult to track down and deal with, so this reduces some of the competition for foreclosure properties. With stamina, determination, people skills, and this book, you have everything you need to tap into this open market.

Tracking down the homeowners

When people can't pay their bills, the repo man is trying to drive off with their car, bill collectors are harassing them, and the phone company has disconnected their service, they can be a little tough to get a hold of. Many distressed homeowners even go into hiding — they refuse to answer the door or the phone, they avoid the neighbors, and sometimes they even up and leave, vacating the premises.

To contact homeowners, you often need to do a little detective work first to find out where they're living and to obtain a phone number, just in case they're answering the phone. Here are some tips that have worked well for me in tracking down homeowners:

- **Contact the county's tax assessor's or treasurer's office (whoever sends out the tax bills).** The address where the tax bills are sent is public information, and the bills go to the homeowner. If the homeowner is not residing at the property, the tax bill may be going to a different address.
- **Send a letter to the property's address with a return receipt request attached to it.** See "Contacting the Homeowners Directly," for some sample letters. If the person is no longer at the address you used, you get the letter back with the person's forwarding address on it. The postal service charges about a buck for the return receipt request.
- **Contact the neighbors.** If you don't have their phone numbers, use a reverse address search tool on the Internet to obtain their phone numbers. At `www.whitepages.com`, for example, you can select the Reverse Address option, enter a person's address, and get the names and phone number of the people residing there.
- **Search for the homeowners by name online at Web sites like `www.whitepages.com`.** Several online services are available for tracking down people that charge a relatively small fee to track down unlisted numbers.
- **Flip through the phone book and call everyone who has the same last name as the person you're trying to contact.** Start with the people who live in the area near the property and fan out.
- **In cases of divorce, you may need to go down to the county courthouse and look up the marriage certificate to find out the wife's maiden name.**

REMEMBER

The more difficult a homeowner is to contact, the better the opportunity for you. Most foreclosure investors give up when their first few attempts to contact the homeowner fail, leaving you with less competition. With a little persistence, you may be the lone investor who succeeds at contacting the homeowner.

Kicking off your mail campaign

Contacting homeowners prior to the auction is not a one-time event. Like a doctor whose treating a patient in recovery, remain in constant contact with the homeowners up until the time they decide how they want to resolve the situation. Your goal should be to contact the homeowners at least once a week via phone, mail, personal visits, e-mail, or a combination of methods. Success in pre-auction foreclosures hinges on your ability to continually let the homeowners know how you can assist them.

Your primary medium for contacting distressed homeowners is the letter — either mailed to the homeowners' address or hand-delivered. In the following sections, I supply you with samples of letters I use, but in most cases, you should edit the letter to give it a more personal touch.

Delivering a letter of introduction

In your first letter, let the homeowners know that you know they are facing foreclosure, that they have options, and that you can provide some guidance. Include your phone number, so they can contact you for additional information and to set up an appointment. Figure 9-1 shows a sample letter of introduction.

TIP

You can type the letter, but hand-address the envelope. If you use your printer to print the mailing address, the letter may appear too official, and the homeowners may not even open it. For your return address, use the address of your business or personal residence — a P.O. box number is too impersonal.

Delivering follow-up letters

Read the foreclosure notices every week, as explained in Chapter 7. If a foreclosure notice is posted for the property in this week's legal news or local paper, send a follow-up letter to the homeowners. You should send a follow-up letter every week leading up to the week of the foreclosure sale.

TIP

With each successive letter, add a touch more urgency in your call to action. Always emphasize that doing nothing is the worst thing anyone in foreclosure can do. Time is of the essence! Figures 9-2, 9-3, and 9-4 provide sample letters you can send to homeowners at the beginning of weeks 2, 3, and 4. Note that each letter increases the sense of urgency.

TIP

Consider sending a letter the day of the sale, informing the homeowner that the house went to sale and that you have the amount it sold for, the name of the person who purchased the property, and the amount of the overbid (if an overbid occurred). An overbid occurs if someone bids more for the property than is needed to cover the amount owed on it; homeowners can claim the overbid money. Let them know how to contact you so that you have another opportunity to personally talk with them, set up a face-to-face meeting, and supply them with this valuable information and what it means.

Congratulating the homeowners

As you're checking the weekly foreclosure notices, you may find that a foreclosure notice does not appear for a property you're tracking. In some cases, the homeowners negotiate a solution with the lender. When this occurs, don't assume that your relationship with the homeowners has ended. Send them a letter of congratulations, as shown in Figure 9-5.

Many homeowners who survive the current financial crisis end up in the same position later down the road. If you've been helpful, they are likely to contact you the next time they experience difficulties. Even if they don't have future problems, they may recommend you to friends or relatives who find themselves in a similar situation.

<Your Address>
<City>, <State> <Zip>
<Date>

<Homeowner's Names>
<Address>
<City>, <State> <Zip>

Dear Friend,

Sometimes bad things happen to good people. I am sorry to learn that the lender who holds your mortgage has begun foreclosing on your home. Despite what you may be hearing from other people trying to make a quick buck at your expense, you may have other options other than losing your home.

I am dedicated to helping people in this area achieve the American dream of homeownership. I am also dedicated to helping people hold onto that dream when they are facing hard times. I am committed to making sure that people in foreclosure know all of the options available to them when facing this situation.

You are not alone. Hundreds of thousands of homeowners in the United States face similar situations every year. Foreclosure is almost epidemic. Most of the people in these situations are just like you—hardworking people who have had a few bad breaks.

I have studied the foreclosure process in our area and can explain your options to you in detail. Some of these options may enable you to retain possession of your house or at least delay the process, so you have more time to seek better solutions and preserve your credit rating. The sooner you take action, the better your options.

Don't lose your home and the equity you've worked so hard to build up just because you're too embarrassed to get advice. I have helped many people in your situation and I can help you too. Please call me at <Your Phone Number>, so we can discuss your options and start putting this nightmare behind you.

The worst thing you can do now is nothing! I can't be forceful enough on this point. If you ignore this problem, you will lose your home. Please call me today.

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

Figure 9-1: Write a letter of introduction, letting the homeowners know how you can assist them.

<Your Address>
<City>, <State> <Zip>
<Date>

<Homeowner's Names>
<Address>
<City>, <State> <Zip>

Dear Friend,
You are receiving this letter because, incredibly, your financial difficulty is now a matter of public record.

I say, "Dear Friend," because I have a good idea what you're going through. My mentor, Ralph Roberts, was in your shoes when he lost his own home back in 1979. He knows what it's like to be angry, frustrated, and hounded by creditors. You wonder if you'll ever get ahead. Ralph hated the ring of the phone, but he hated it even more when they shut off his phone.

Today, 20 years after his ordeal, Ralph will tell you that he lost his home because he was too embarrassed to ask for help. He lost his home because he did nothing and allowed it to be taken from him without even putting up a fight. Fortunately for you, however, that horrible experience motivated Ralph to do everything he could to make sure other people—good people like you—don't have to go through the same thing he did.

That is why Ralph began training investors all over the country to help people in foreclosure. He studied foreclosures throughout North America to learn about every possible option available to people facing this nightmare. With Ralph's training and consultation, I have developed a system—a step-by-step strategy –for helping people like you to escape the trap of foreclosure.

This system has worked for countless others across the country. I'm sure it can work for you if you'll just give me the chance to help you out.

With my assistance, you can successfully navigate the foreclosure process. I'm sure you don't realize the many options you do have available to you. In many cases, if you act quickly, you can keep your home. If that's not possible, you can at least receive fair market value for the property, protect your credit rating, and avoid seeing your house sold to the highest bidder at a Sheriff's Sale.

I am here—ready, willing and able to help. But YOU have to make the first move and give me a call. Please call me directly at <Your Phone Number>, so we get started putting this nightmare behind you.

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

P.S. As I mentioned above, you do have many options available to you. But, the longer you wait, the fewer options you will have. And, if you sit and do nothing, you will lose your home. Please do something to help yourself and call me today.

Figure 9-2: Write a follow-up letter for the second week.

<Your Address>
<City>, <State> <Zip>
<Date>

<Homeowner's Names>
<Address>
<City>, <State> <Zip>

Dear Friend,

The Sheriff's Sale on <Mortgage Sale Date> is fast approaching.

I am extremely concerned!

This is the third letter I've sent you—yet I still haven't heard back from you. Just so that you are completely aware of what's going on here, I believe that it is very important that you fully understand what will happen if your house goes to that Sheriff's Sale.

At the Sheriff's Sale, your property will be sold to the highest bidder. If no investor comes forward to bid on your property, it will be turned over to the bank that holds your mortgage. Either way, you will have no right to reinstate your existing mortgage once the sale takes place.

If you continue to do nothing, you WILL lose your home. That is a harsh statement, but I want to be perfectly clear so that I know you are completely aware of your situation and the consequences of your actions—or inaction.

Please, call me directly at <Your Phone Number> to let me know that you do indeed understand what is going to happen. If you call me right away, you still have options available to you. But realize that your time is quickly running out.

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

P.S. If you want to save what equity you have in your home—not to mention your credit rating—doing nothing is NOT an option. Please call me TODAY before it's too late. Don't let embarrassment about your situation cause you to lose your home; I've helped many good people, just like you, turn things around.

Figure 9-3: Write a follow-up letter for the third week.

<Your Address>
<City>, <State> <Zip>
<Date>

<Homeowner's Names>
<Address>
<City>, <State> <Zip>

Dear Friend,

You are almost out of time.

You have only a few days until your home will be sold to the highest bidder at the Sheriff's Sale. Unless you do something immediately, someone else will own your home within the week.

Believe it or not, you still have options available to you. If you'll just take the first step and give me a call, I have all the knowledge, resources, and expertise available to help you escape your foreclosure nightmare and get your life back on track. But, unfortunately, I am powerless to help you—UNLESS you call me RIGHT NOW!

If you do nothing, you WILL lose your home. The sad part is that you don't have to.

Right now you probably feel totally alone, as if you don't have a friend in the world. But, in reality, you have a friend right here who is ready, willing, and able to help. I know what you're going through.

My mentor, the best-selling Realtor in America, Ralph Roberts himself lost his own home to foreclosure back in 1979. That is why he has taught me all about foreclosures so I can help people like you—good people who have had some bad breaks. I have helped many people facing the same situation as you. I CAN help you, too.

Please call me NOW at <Your Phone Number>.

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

P.S. People facing foreclosure commonly remain in denial about this horrible thing that is happening to them. But, unfortunately, time is working against you. If you continue to do nothing, IN A FEW DAYS SOMEONE ELSE WILL OWN YOUR HOME. Please, please call me NOW so I can help!

Figure 9-4: Write a follow-up letter for the fourth week.

<Your Address>
<City>, <State> <Zip>
<Date>

<Homeowner's Names>
<Address>
<City>, <State> <Zip>

Dear <Homeowners' First Names>,

I was happy to see that you were able to reinstate your loan with <Lender's Name>. I know that the past few months have been terribly stressful for you and your family. I hope the information outlining the options available to people facing foreclosure that I've sent to you over the past few weeks has been helpful.

If you, or anyone you know, ever faces a similar situation, please don't hesitate to call me. I am happy to help in any way I can. I've enclosed a few of my business cards just in case you meet someone who needs my assistance. I wish you the best!

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

Figure 9-5: Congratulate the homeowners if they work out a solution with their lenders.

Getting in touch over the phone

Through your letter campaign, hopefully the homeowners call you, but if they haven't called by the second week, try giving them a ring. When you eventually do get in touch with them, your goal is to set up an initial face-to-face meeting at their kitchen table. Be prepared to listen closely to what they say and take notes. Figure 9-6 provides a sample phone script you can use to guide you through your initial conversation with the homeowners.

Be prepared to field calls at any time of the day or night from people who are afraid. You should have a cell phone and be very accessible. I've received phone calls well into the wee hours of the morning. Distressed homeowners seem to gain their courage as the sun sets. Many spouses call when their husband or wife are at work or sleeping. Keep in mind that these callers do not know what to do, and they may be dealing with other tragic situations, so this often results in an atmosphere of uneasiness.

You say: Hello, my name is <Your Name>. I'm a real estate investor who helps homeowners just like you escape the foreclosure trap. I have been trying to reach you for some time now. As crazy as it sounds, the fact that you're facing foreclosure is now a matter of public record.

Despite what others who have already contacted you may have told you, you do have rights and options available to you to save your home.

I would like to get together with you as soon as possible to discuss your options. Can we meet at your house or at my office sometime this week?

Homeowner says: Yes.

You say: Fantastic, let me know what's best for you. (Set up an appointment.)

Homeowner says: No.

You say: I think you owe it to yourself to at least find out how the foreclosure process works and what rights you have so people don't try to take advantage of you. Will you at least take a few minutes right now to let me tell you about your rights?

Homeowner says: Yes.

You say: Believe me, you are doing the right thing. I've helped a lot of people save their homes and credit ratings. How many months are you behind on your mortgage? Tell me a little about how you got into this situation. (Ask questions from the homeowner information sheet shown in Figure 10-6.)

Homeowner says: No.

You say: If you change your mind—and I really hope you do—give me a call. I would definitely be willing to give you a second opinion on any deals that someone else offers you. My name and number are <Your Name> <Your Phone Number>.

Figure 9-6: This phone script can guide you through your first conversation with the homeowners.

Don't forget to include the spouse if a couple owns the home. Early on in your conversation, ask if the spouse knows of the situation. Eventually, the spouse needs to be brought into the discussion, but you want to make sure it's done properly. I've had spouses ask me to be the bearer of bad news, but the partner should have the option of breaking the bad news himself. Once both homeowners are apprised of what's going on, they need to both be included in the decision process and the signing of any agreements.

Before you call, brush up on the options available to the homeowners, just in case they ask about them. Ideally, your phone call results in a face-to-face meeting with the homeowners, but if they ask about their options, be prepared to provide some general information. For details about homeowners' options, see "Laying Out All Available Options," later in this chapter.

As you converse, keep the following tips in mind:

- Realize that the homeowners may have already been contacted by others.
- Listen more than you talk and show compassion for their situation. The homeowners can really use a sympathetic ear, and hearing their story provides you with valuable background information about their situation and mindset. This is your opportunity to establish a bond of trust.
- Let the homeowners know that you want to assist them and are an expert in foreclosure options.
- Emphasize that the worst action they can take is to do nothing.
- Ask lots of questions, but don't interrupt. They have to know that you care before they'll care what you know. Interrupting someone who is pouring out their heart is potentially devastating to your relationship. Remember that something you feel is important can seem *completely unimportant* to someone whose emotions are ruling his thoughts.

Your initial conversation is a success if you achieve the following goals:

- Obtain the homeowners' complete contact information.
- Establish yourself as an expert in foreclosure matters.
- Let the homeowners know that they have options and that you can explain their options when you meet for the first time.
- Assist the homeowners in understanding their rights and the foreclosure process. In Michigan, for example, few homeowners realize that they control the home through the redemption period.
- Inform the homeowners that they need to be very careful, because unsavory characters may purposely mislead them to take advantage of them.
- Schedule a face-to-face meeting.
- Instruct the homeowners to gather all the paperwork related to the property, including the closing package they received when they purchased the property, correspondence from the lender and the foreclosing attorney, and (if available) any notices posted on the property by the sheriff.

Once you've set up a meeting, ask the homeowners why they called you instead of talking with another investor, and ask to see any correspondence they received from other investors. Get to know the people you're competing against and what you're doing that works and doesn't work.

Adding the Homeowners' Profile to Your Property Dossier

In order to assess the homeowners' current foreclosure situation, you first need to gather some essential details. When you meet with the homeowners for the first time, explain the foreclosure process and ask the following questions:

- How did the situation escalate to this point?
- Have you discussed your situation with any other professionals, such as agents, lawyers, accountants, lenders?
- If you discussed the situation with others, what did they suggest?
- What do you want to do? Save your house? Save your equity and move? File for bankruptcy? (When mentioning bankruptcy, stress that you are not an attorney and cannot provide legal advice or representation. You can, however, share general information about the different types of bankruptcy.)
- Can I take some time to explain your options? (Remember that options vary depending on the amount of time the homeowners have to act and the amount of equity they have built up in the property.)
- Do you have any questions about your rights and options?

When you've gained the homeowners' trust, explain that to help them you need to know some more detailed information. Work with the homeowners to complete the homeowner information sheet shown in Figure 9-7.

Laying Out All Available Options

Once you've completed the foreclosure information sheet (Chapter 7) and the homeowner information sheet (Figure 9-7) and have a first-hand account of the situation, the homeowners' situation becomes much clearer. You begin to get a sense of what the owners want to do, what options they can realistically accomplish, and which is the best course of action for them to take, whether it's refinancing, selling, downsizing, renting or, in the worst cases, filing for bankruptcy.

Name: ______________________________

Address: ______________________________

Home Phone: __________ Work Phone: __________ Pager/Mobile: __________

How long have you lived in the house? ______________________________

Marital Status: ☐ Single ☐ Married ☐ Divorced

Is your spouse aware of this situation? ☐ Yes ☐ No

Number of Children: __________ Ages of Children: __________

Occupation: __________ Employer: __________

What made you decide to contact me? ______________________________

Why are you in foreclosure? ______________________________

____

Gross Income: ______________________________

Foreclosure Sale Date: __________ Redemption Period: __________

Type of loan: ☐ Conventional ☐ FHA ☐ VA ☐ Other: __________

Loan Balance: __________ Interest Rate: __________

Monthly house payment: __________ No. of months behind: __________

How much are you comfortable paying each month? ______________________________

How much do you have in available cash or liquid assets? ______________________________

Can you borrow from family or friends? ☐ No ☐ Yes, how much? __________

Owner's estimated value of home: ______________________________

Do you have any: ☐ Second mortgages ☐ Tax liens ☐ Mechanic's liens

Been in foreclosure before? ☐ Yes ☐ No

Now in or ever filed for bankruptcy before? ☐ No ☐ Yes

If yes, what type? ☐ Chapter 7 ☐ Chapter 13

Bankruptcy details: ☐ Currently in ☐ Completed on: __________

Others consulted: ☐ Bank/Mortgage Co. ☐ Attorney ☐ Realtor

☐ Accountant ☐ Others: __________

What advice did they give you? ______________________________

____

What would you like to see happen to your home? ______________________________

____

When can I come to see the property? ______________________________

What Owner Wants: ☐ Cash Buy ☐ Re-Fi ☐ List ☐ Short Sale ☐ Other

Reasoning/Notes: ______________________________

____

____

Figure 9-7: Gather information from the homeowners.

In the following sections, I describe the various options available, so you can understand them and present them to the homeowners. I also show you how to rule out unrealistic options based on the homeowners' situation.

Reinstating the loan

If the homeowners can come up with enough cash to bring their mortgage payments up to date and pay any back taxes and penalties, they may be able to reinstate the mortgage. In most cases, this requires that the homeowners sell other assets or obtain financial assistance from family or friends.

Most homeowners in foreclosure are too embarrassed to ask family and friends for help, but this is often the best solution. Encourage the homeowners to contact any family members who may be able to give or loan them the money to pay off the lender who's foreclosing on the property. In many cases, I meet with family members personally to assist the homeowner in telling family members about their situation.

Convincing the homeowners to seek help

Convincing distressed homeowners to seek assistance from family members is a challenge. You can often succeed by asking the homeowners what they would do if they were in a position to help someone in their family who was experiencing financial problems.

My office was once in the process of assisting a young couple who had three small children. Initially, I met with the wife at her home. Once she felt comfortable, she and her husband came to the office.

As I began laying out their options, the first option I presented was to ask friends and family to help. I explained that homeowners in similar situations often have people in their lives who can help, but because of shame or embarrassment, most homeowners won't ask for help. I asked if they had anyone they could go to for some financial assistance. They explained that they didn't want to ask friends or family for help.

Then I asked them that if a loved one needed help and they had the means to help that person, how would they feel if they weren't asked. The couple continued to refuse to ask friends or family for help.

I continued explaining their remaining options. After each option, I asked them if the option was something they thought would fit their situation better. The husband became a bit uneasy and said that they actually did have someone they could go to, but his wife was unwilling.

After some discussion, I learned that the wife's parents were very wealthy and owned a thriving business on the East Coast. She didn't want to call because she was afraid that her father would be mad. I told her that her father would probably be mad because she hadn't called him earlier, and that he would probably be more upset to know that his grandchildren were needlessly evicted. I also asked, "If one of your children needed help, wouldn't you want to be called immediately?"

The answer of course was "Yes," and we called her parents right then from our conference room. All of the emotions that you would expect poured out during that phone conversation, and the couple worked through a very painful experience, but it resulted in saving their home.

Negotiating with the lenders for a forbearance

If the homeowners have experienced a temporary financial setback, they may be able to work out a solution with the lender to restructure their payments and get back on track. If they've fallen way behind in their payments and their prospects of getting back on track look bleak, however, the lender is unlikely to agree to a forbearance.

TIP

With the homeowners' approval and a signed release form, like the one shown in Figure 9-8, you can negotiate with the lender on the homeowners' behalf to agree to a forbearance. Remember, however, that you won't be the one sending the check to the lender each week, so the homeowner has to be on board and able to perform or else you will have lost credibility with that lender the next time you call.

<Your Address>
<City. State, Zip>

Borrower Certification &
Authorization to Release Information

1. I/We authorize you to provide <Your Name or Business Name> its representatives, successors, and/or assignees, any and all information and/or documentation that they might reasonably request. Such information includes, but is not limited to employment history and income; bank, money market, and similar account balances; credit history; and copies of income tax returns.

2. I/We further authorize <Your Name or Business Name> its representatives, successors, and/or assignees to request a credit report and all credit information required by <Your Name or Business Name>.

3. A copy of this authorization, including a facsimile transmission, may be accepted as an original.

X________________	________________	________________
Borrower	Date	Social Security Number
X________________	________________	________________
Borrower	Date	Social Security Number

Figure 9-8: Ask the homeowners to sign a statement giving you permission to discuss the situation with lenders.

Refinancing the mortgage

For homeowners with solid, stable incomes and assets other than their home who are experiencing a temporary financial setback, refinancing to a *nonconforming* loan may be an option. A nonconforming loan is a mortgage that typically charges 2–3 percent interest above conventional rates plus additional points at closing. In some cases, if the homeowners can make their payments on time for a year, they qualify for refinancing back to a conforming mortgage.

Refinancing is usually a poor choice for people with lower incomes, because even if they qualify for a nonconforming loan, they may end up having higher monthly mortgage payments than what they previously had. Refinancing simply sets them up for another round of foreclosure.

If the homeowners' gross income is sufficient for covering their monthly bills in addition to a higher monthly mortgage payment, offer to set up a meeting with your loan officer to discuss their options with them. But hurry, the clock is ticking!

Listing the property

Homeowners who have several thousands of dollars worth of equity built up in their homes are often best served by placing the house on the market, selling it, and moving to more affordable accommodations. This option enables the homeowners to keep much or all of the equity they've accumulated in their home. Unfortunately, this is usually the last option they're willing to consider.

When presenting this option to homeowners, highlight the following key points:

- If the homeowners have little, no, or negative equity in the property, this option is off the table.
- If the auction is scheduled to occur in the next few weeks, the homeowners may not be able to sell it in time. If, however, your area has a lengthy redemption period, they do have time to sell.
- If the homeowners are already in their redemption period, remind them that interest is accruing on the amount the bank or investor paid for the mortgage at the auction. The sooner they sell, the less interest they pay.

- To sell the home faster, recommend that the homeowners sell through a qualified real estate agent, and make sure that the agent they pick understands foreclosure and that time is of the essence.
- If the homeowners are reluctant to sell just because "it's their home," remind them that it is only a house and that the next house they move into will provide the same opportunities to create wonderful memories. This is a harder obstacle to overcome when the house has been in the family for many years or generations.

TIP

Sometimes, you can convince the homeowners to list their house right away by explaining that having more time to market the home gives them a better chance of selling it for full market value. Waiting to list could back the owners into the corner of being forced to accept less than market value or losing their home outright. Keep in mind that they may need time following the offer for a buyer to get financing and for the closing packages to be put together.

Selling short

When the homeowners owe more on a home than what they can sell it for, you can sometimes work a short sale with the lending institution. In a short sale, the bank may accept less money than what is owed in order to get the bad loan off its books, letting the homeowners off the hook. For details about short sales, consult Chapter 15. (Negotiating a short sale takes time and patience.)

Accepting your cash offer

When homeowners want to sell their home but they don't have sufficient time to sell it for market value or are not interested in going through the hassle of selling their home, selling the house to you for cash is often a very attractive option. The more equity the homeowners have in the house, the more cash you can offer them for the property. In the event that one of the homeowners died or a couple divorced, cash is often even more appealing.

To decide how much to offer for a property, check out Chapter 10.

Refinancing through you

In some situations, refinancing the mortgage through you is the best option for the homeowners. This is often the case if the homeowners lost the property in foreclosure but still have an opportunity to redeem it. Because they now have a foreclosure on their credit history, they may not qualify for a loan or the interest rates may be cost prohibitive, even if they can now afford the monthly payments.

Consider this somewhat common scenario. The homeowner loses his job, loses the property at the foreclosure sale, and then gets another job that enables him to afford the monthly payment. The homeowner can't get loan approval because of the foreclosure. Here's where you step in. You buy the property and sell it back to the owners on a land contract, trust deed, or some other form of seller financing.

By offering an interest rate several percentage points below what they would probably pay on a non-conforming loan from an equity lender (assuming they could even quality for such a loan), they could keep their monthly payment near their current level or even lower it and stay in their home. Over time, they may even be able to rebuild their credit history and qualify for a conventional loan at a lower interest.

Your state probably has a cap on the interest you can charge on land contracts. Make sure you know the rules. You don't want to be in violation of any usury laws (prohibiting unfair lending practices).

For additional information and tips on how to sell a home back to the homeowners, check out Chapter 19.

Leasing the property after selling it

Homeowners who are high credit risks — they have bad credit history, low income, questionable job security, and little or no assets — may be able to afford to buy back the home with a rent-to-own arrangement known as a *lease-option* deal.

In a lease-option deal, you purchase the property and lease it back to the former owners, providing them with the option of buying it back later, if they meet the criteria outlined in the agreement. You may or may not want to apply all or a portion of the lease payments toward the purchase price if your customers exercise their option. See Chapter 18 for more information about lease-option deals.

Selling the home and renting it back

When homeowners can no longer afford their monthly mortgage payments and refuse any option that requires them to vacate the premises, you may consider buying the property and leasing it back to them. After some time, you can present your tenants with a couple other options:

- Purchase a less expensive house from you in the same area.
- Purchase the house back from you or sign a lease-option agreement that enables them to rent-to-own.

WARNING!

Establish rental relationships only with homeowners who've shown that they've been taking good care of the property and can afford to pay enough rent to make the relationship profitable for you. Carefully evaluate their financial position to make sure they can afford the rent. You don't want to put yourself in the position of having to evict your tenants two months down the road. For more about leasing the property back to the homeowners, see Chapter 18.

Giving a deed in lieu of foreclosure

When the homeowner owes more on a property than what it's worth and the lender refuses to agree to a short sale, the best option for the homeowners may be to offer the lender the *deed in lieu of foreclosure.* When homeowners give a deed in lieu foreclosure, they relinquish ownership of the home and walk away.

Offering a deed in lieu of foreclosure is better than foreclosure. It's the right thing to do, if no other options make sense and the lender agrees to go along with it. The lender may even report the mortgage as paid as agreed, but there's no guarantee. In some cases, the lender refuses to accept the deed; for example, if the property is condemned or has some sort of environmental problems or if the owners have other assets that the lender wants to go after.

WARNING!

If the homeowners have little, no, or negative equity in the property, they may be willing to deed the property to you in exchange for your paying off the balance of the mortgage. They do this by signing a *quit claim deed.* If you accept a quit claim deed, pay off the mortgage immediately. Real estate con artists often convince homeowners to sign a quit claim deed, promise to pay off the mortgage, and never do.

REMEMBER

Giving the deed in lieu of foreclosure only makes sense if the homeowners have negative equity in the home and are near the end of the foreclosure process. If the homeowners have time prior to the auction or during the redemption period, they should seek other options first, such as negotiating a short sale or selling the property themselves. Some mortgage companies will pay for a deed in lieu of foreclosure, this may make the option more appealing to the homeowners.

Filing for bankruptcy

Bankruptcy is the option of last resort. Usually it is just a quick-fix solution that only temporarily prevents the mortgage sale. When someone files bankruptcy the court issues a *stay* that stops all actions. Many lending institutions simply adjourn the foreclosure proceedings until the owner is out of bankruptcy or until they can convince the court to lift the *stay.* The owners end up with the same problems that drove them into bankruptcy, plus they now have attorney fees and trustee fees to pay.

Bankruptcy, however, can be an effective tool for wiping out junior liens on a property. This is where your relationships with bankruptcy attorneys can be helpful to your customers. If a customer starts talking about bankruptcy, clearly state that you're not an attorney (unless you actually are one) and that you believe they should talk about that option with a lawyer.

If the homeowners decide to file for bankruptcy, make sure they see a reputable attorney. Cheap, fly-by-night legal services, commonly referred to as *mills,* can churn out the necessary paperwork, but they don't provide the appropriate personal advice. Encourage the homeowners to seek out a bankruptcy trustee or, at the very least, have several consultations with different attorneys.

Waiting (and saving) during redemption

If you're working the foreclosure circuit in an area with a somewhat generous redemption period (at least three months), the homeowners have the option of continuing to live in the house for the duration of the redemption period without having to pay their monthly mortgage.

In addition to buying them some time to explore options, if the homeowners can set aside the money they would normally be paying on the mortgage, they can sock away enough cash to pay a security deposit on a lease or to cover an option fee to purchase a more affordable property on a lease-option contract, as explained in Chapter 18. The problem with this option is that homeowners whose finances are already strained may not be able to actually set the money aside. I have seen situations in which homeowners were very successful with this strategy, so you should present it as an option.

Doing nothing

While doing nothing isn't really an option, unfortunately, it's a course of action most people in foreclosure choose to take. It's actually the worst possible thing to do. Doing nothing ultimately leads to the homeowners losing their home, any equity they have built up in it, and their ability to qualify for future financing.

Constantly remind homeowners who are facing foreclosure that doing nothing is the absolute worst course of action . . . or is it inaction? Once they lose their house, they have no other option but to move and are in a terrible position to do even that effectively.

Getting Inside to Take a Look Around

At some point in your dealings with the homeowners, try to get inside the home to inspect it. If you do end up trying to buy the property from the homeowners or later at auction, you should know the condition of what you're buying. If possible, inspect the home, and complete the home interior inspection form, shown in Figure 9-9.

If you're a real estate agent purchasing the home at a price below market value, you're probably required by the laws and regulations in your state to inform the homeowner of this fact. Have the homeowners sign a statement that you informed them that you're purchasing the house below market value, and that the deal was advantageous to them because you could cash them out quickly without any of the hassles associated with listing and selling.

Contacting the Lenders

When homeowners take out loans, they enter into legal contracts, similar in some ways to wedding vows. As a foreclosure specialist, you may take on the role of mediator when the marriage takes a turn for the worse. As mediator, your job is to establish some sort of communication between the two parties that resolves their current dispute.

You can call lenders to inform them that you are interested in the property and willing to make deals with them during the foreclosure process, but in order to mediate effectively between the homeowners and lenders, you must have written permission from the homeowners. Figure 9-8 provides a permission form for the homeowners to sign.

Interior Property Evaluation

Owner: ____________________

Home Phone: __________ Work Phone: __________ Pager/Mobile: __________

Address: ____________________

Cross Streets: ____________________

Occupant reported problems:

❑ Electrical ❑ Plumbing ❑ Heating ❑ Leaks ❑ Others: __________

Details: ____________________

KITCHEN

Check: ❑ Water Pressure ❑ Lights ❑ Floor ❑ Cabinets ❑ Counter Tops ❑ Sink

Overall Condition: ❑ Poor ❑ Fair ❑ Good ❑ Excellent

Kitchen Notes: ____________________

____

BATHROOM

Check: ❑ Water Pressure ❑ Lights ❑ Floor ❑ Sink ❑ Tub/Shower ❑ Mirror ❑ Vanity

Overall Condition: ❑ Poor ❑ Fair ❑ Good ❑ Excellent

Bathroom Notes: ____________________

____

OTHER ROOMS (Living Room / Bedrooms / Family Room / Den / Library / etc.)

Check: ❑ Floor Covering ❑ Paint/Wallpaper ❑ Ceiling

Overall Condition: ❑ Poor ❑ Fair ❑ Good ❑ Excellent

Other Rooms Notes: ____________________

____

Interior Extras: ____________________

BASEMENT

Check: ❑ Cracks in Walls & Floor ❑ Windows ❑ Watertight? ❑ Stairs/Handrail ❑ Lights

Overall Condition: ❑ Poor ❑ Fair ❑ Good ❑ Excellent

Basement Notes: ____________________

____

Recommendation: ❑ Cash Buy ❑ Re-Fi ❑ Listing ❑ Short Sale ❑ Pass ❑ Other: __________

Reasoning/Notes: ____________________

____

Figure 9-9: Inspect the home's interior, if possible.

Contacting the senior lien holder

The senior lien holder (who holds the first mortgage) has the strongest position, because they stand to take possession of the property if the homeowners don't act and nobody buys the property at auction. Most lenders don't want to take possession of a property, so they're often very motivated to resolve the situation before the sale.

You can get in touch with the lenders either through the foreclosing attorney (listed on the foreclosure notice) or by obtaining the lender's phone number from the homeowners, if you're working with them directly. In some cases, the bank that made the loan has a loan servicer who processes the payments. You may need to call the loan servicer to obtain the lender's phone number.

TIP

Negotiation with big-time national lenders usually is not an option. It's a better strategy if you're dealing with local lenders or credit unions — especially if you've established a relationship with them.

Ask the lender or attorney whether the homeowners have the following options:

- **Reinstatement:** How much would the homeowners have to pay and on what date to have the loan reinstated?
- **Forbearance:** Is the lender willing to work with the homeowners to restructure the payments and perhaps delay payment for a period of time to enable the homeowners to establish their financial footing? What can they offer?
- **Short sale:** Is the lender willing to accept something less than the full mortgage amount currently due?

TIP

When negotiating a short sale, you usually need to make an offer of how much the homeowners or you are willing to pay. Work the numbers as explained in Chapter 10. You can often strengthen your position by having an appraisal or an offer to purchase the property that shows the lender that she's unlikely to get more money than you are offering if the lender goes through with the foreclosure. When submitting an offer, send it to both the lender and the foreclosing attorney, so all interested parties are aware of your offer.

Contacting the junior lien holders

Any lien holder can lay claim to a property for the payment of an unpaid debt. Even if you purchase the senior lien, a junior lien holder may choose to redeem your lien in order to protect his interest. The more effectively you can negotiate with these lien holders from your position of power as the senior lien holder, the more likely you can ultimately take possession of the property uncontested.

Because junior lien holders are likely to have their liens wiped out at the foreclosure sale, they're usually much more willing to negotiate. When you call junior lien holders, let them know the following:

- Their claim may be wiped out during foreclosure proceedings.
- You are willing to work deals with them.
- You will let them know when you find their interests at risk because of foreclosure proceedings on future properties.
- You would like the opportunity to list any properties they plan on selling.

Junior lien holders are often willing to accept payments of 50–80 percent less than what they're owed, but your strategy my vary depending on whether your state has a redemption period:

- In states with no redemption period, you have more power to negotiate in the days leading up to the auction, because if the property ends up selling at auction, any junior liens are wiped out and the junior lien holders often stand to get nothing.
- In states with a redemption period, you gain bargaining power the closer you get to the last day of the redemption period, because if the junior lien holder has only two options — accept a payout from you or redeem your position and end up with a house he may not want the hassle of fixing up and selling.

For details about junior liens and information on how to negotiate short sales, skip ahead to Chapter 15.

Chapter 10

Analyzing the Deal and Presenting Your Offer

In This Chapter

- Filling out the deal analysis worksheet
- Analyzing the homeowners' position
- Listing the homeowners' most feasible options
- Preparing and presenting a purchase agreement

At least three parties share an interest in the outcome of the pre-auction foreclosure — the homeowners, the lenders, and you. As a foreclosure investor, your mission is to craft a deal that satisfies all three parties. The homeowners may salvage their credit and cash out some or all of the equity in the property, the lenders trim their losses to a satisfactory amount and remove the bad loan from their books, and you walk away with the property or a consulting fee and the satisfaction of having done a good deed.

In this chapter, I show you how to take the information you gathered in Chapters 7 and 9 and any additional information you may have collected on your own and complete a deal analysis worksheet. With this worksheet in hand, you can determine which options are best for the homeowner, for the lenders, and for yourself.

If the homeowners decide to accept a cash offer from you, I show you the basics of drawing up a purchase agreement to make the transaction official and closing on the deal.

Completing the Deal Analysis Worksheet

With the foreclosure information sheet and exterior inspection report from Chapter 7 and the homeowner information sheet and interior inspection report from Chapter 9, you now have the details you need to analyze the deal and determine which options are best for the homeowners, the lien holders, and yourself.

The deal analysis worksheet, shown in Figure 10-1, assists you in consolidating the information you gathered and analyzing that information. In the following sections, I lead you through the worksheet and explain the significance of each of its sections. For now, complete the first three lines of the worksheet to record the homeowners' names, the property address, and the homeowners' home, work, and mobile phone numbers.

Calculating the homeowners' equity in the property

As a property increases in value and you pay down the principle on the mortgage, you build up *equity* in the property. Equity is the amount of money you'd have if you sold the property and paid off the total amount you borrowed against the property.

By knowing ahead of time exactly how much a property is worth and how much the homeowners owe on it, you can calculate a rough estimate of the equity they have built up in the property and be in a better position to assess their situation and present them with viable options.

TIP

The less equity a homeowner has in a property, the less attractive are the homeowner's options. With little, no, or negative equity, the homeowners are likely to lose the property and walk away with nothing. Homeowners facing foreclosure often are unaware of the power of the equity they have in their homes. You may have to explain what equity is and how it can open up their options to them. However, if they wait too long, and the property is auctioned off, they can end up losing all of their hard-earned equity.

Guesstimating the "as is" market value

The market value of a property is always a best-guess estimate. As most real estate agents can tell you, a property's value is equivalent to whatever a buyer is willing to pay for it and a seller is willing to sell it for. To evaluate the market and estimate a realistic resale value, research the following and add the results of your research to your property dossier:

- Actual sales prices of comparable homes that have recently sold in the same area.
- Asking prices of comparable homes currently for sale in the same area.

Deal Analysis Worksheet

Homeowner Name: ____________________

Property Address: ____________________

Home Phone: __________ Work: __________ Mobile: __________

Market Value As Is: $ __________ Total Liens: $ __________

Homeowners' Equity: $ ____________________

Improved Market Value: $ __________ Repairs/Renovations: $ __________

Purchase Costs: $ __________ Holding Costs: $ __________

Sales Costs: $ __________ Top Cash Offer: $ __________

Loan Status

❑ Delinquent—Foreclosure – Sale Date: ____________________

❑ REJ—Redemption Date: ____________________

❑ Terminal—Cash buy only safe option

LTV

❑ Low – Options:	❑ Cash Buy	❑ Re-Fi	❑ List
❑ Marginal – Options:	❑ Re-Fi	❑ List	❑ Pass
❑ High – Options:	❑ List	❑ Short Sale Negotiation	

Homeowner Credit

Does homeowner make payments in a timely manner?	❑ YES	❑ NO
Does homeowner have some bad credit?	❑ YES	❑ NO
Any judgments, collections, tax liens on credit report?	❑ YES	❑ NO
Any bankruptcy?	❑ YES	❑ NO
Was bad credit a one-time problem?	❑ YES	❑ NO

Homeowner Mentality

❑ Wants to keep home ❑ Wants to get rid of home ❑ Relocating

❑ CANNOT afford payments ❑ CAN afford payments up to: $ __________

Homeowner Status

❑ Employed Gross Income: $ ____________________

❑ Unemployed ❑ Going through divorce

Course of Action

❑ Reinstate	❑ Forbearance	❑ Refinance	❑ List	❑ Sell Short
❑ Cash Offer	❑ Lease-option	❑ Sell-and-Rent	❑ 2nd Mortgage	
❑ Deed in Lieu of Foreclosure		❑ Bankruptcy	❑ Nothing/Pass	

❑ Track through Foreclosure Sale ❑ Other: ____________________

Reasoning/Notes: ____________________

____

____

____

I/We, the homeowners have read and understand the options described above.

X ____________________ ____________________

Homeowner Date

X ____________________ ____________________

Homeowner Date

Figure 10-1: Complete the deal analysis worksheet.

TIP

While checking the recent sales prices of comparable homes, check the health of the market, too. Look at the number of sales per month and sales values of comparable homes over the last six months, three months, and 30 days. A steady increase in sales volume and prices is a great sign. If the numbers are flat, the market is in decent shape. If you see a large volume of sales six months ago but few over the last 30 to 60 days, that may indicate a slowing market you should either avoid (until it bottoms out) or account for when you purchase properties.

If you're not too sure about your ability to assess the market value of a particular property, consult a real estate agent in the area. An appraiser may be able to provide an estimated market value, but if he can't get inside to inspect the condition of the property, his guess is probably no better than yours.

You can check the market value of comparable homes in your area online at sites like `HurryHome.com` or `Zillow.com`, but obtaining MLS listings from a real estate agent in the area typically provides you with the most recent and accurate sales figures for comparable properties.

REMEMBER

Real estate agents work on commission. Don't waste their time by having them run comparables without steering some paying work their way. You may have more success by telling the agent that you will eventually list the property with him in return for his work up front. That way he feels as if he's generating business and not just being used for his access to the MLS.

Calculating the amount owed on the property

Calculating the amount that the homeowners currently owe on their home is fairly easy, assuming you know of all the liens on the property. With the assistance and permission of the homeowners, you can call the lien holders and find out how much the homeowners currently owe on each loan. For tips on how to obtain the homeowners' permission to contact their lenders, see Chapter 9.

If you can't get permission, you can still come close by adding up all the liens and subtracting any principle the homeowners are likely to have paid down. If in doubt, default to the face value of the liens (assume no payments were made). Your estimate is likely to be high, but it gives you a number to work from.

Tally up the numbers, and you know how much the homeowners owe in total. Now, subtract the total from the home's estimated market value, and you have the amount of equity built up in the property.

Calculating your top cash offer

Your goal in any real estate investment property should be to earn no less than 20 percent on your total investment. In other words, you should be fairly certain that you can sell the property for 20 percent more than the entire amount of money you've invested in it, including:

- Amount paid for the property
- Payments to lien holders to pay off loans and back taxes
- Cost of repairs and renovations
- Holding costs (monthly loan interest, taxes, insurance, and utilities) to cover the time between when you buy the property and when you sell it
- Costs of buying and selling the property

TIP

Don't be blind to opportunities just because they don't ring the magical 20 percent bell. You need a tighter budget to profit on low-priced properties, but when you're dealing with million dollar properties, a 15-percent return may be worth exploring. When investing in these ritzy neighborhoods, however, keep in mind that putting all your eggs in one basket may be risky and often ties up a lot of cash. Know what you're getting into before you get into it.

Take the following steps to calculate your top cash offer:

1. **Guesstimate how much you can sell the house for after repairs and renovations.** (Base your guess on the recent sales prices of comparable homes in the same area. Guess low on price and high on costs.)
2. **Multiply the amount from Step 1 by one of the following:**
   - .80 in a market where homes values are rising
   - .70 to .75 in a market where home values are steady
   - .65 to .75 in a market where home values are declining
   - .50 to .65 depending on the percentage profit you want to make
3. **Subtract the amount of money required to pay off back taxes and other liens.**
4. **Subtract the closing costs for purchasing the property.**
5. **Subtract renovation expenses × 1.2 (to add 20 percent for unexpected cost overruns).**

6. **Subtract monthly holding costs (interest, insurance, property taxes, utilities) times the number of months you plan on owning the house.** Figure on at least three months.
7. **Subtract agent commissions and/or marketing and advertising costs.**
8. **Subtract closing costs for selling the property.**

The resulting dollar figure is the maximum amount of cash you can pay for the property to be fairly certain of earning a 20 percent profit.

Logging the loan status

Under Loan Status, check the box next to the option that represents the current status of the mortgage that's in foreclosure:

- **Delinquent:** The payment is delinquent, the lender is foreclosing, and a date has been set for the sale.
- **REJ — Redemption:** REJ stands for Real Estate in Judgment. The foreclosure sale already occurred, and the homeowners are currently in the redemption period.
- **Terminal:** The homeowners have run out of options, and the only option left is for them to sell the property to an investor.

Determining options based on LTV (loan-to-value)

To evaluate the risk level of a loan, lenders often evaluate the LTV (loan-to-value) — the amount of the loan compared to the value of the property. The lower the LTV, the less the risk. For example, an LTV of 40 percent on a $200,000 property means that the owners owe only $80,000. If they default on the loan, the bank has a pretty good chance of recouping the full amount they borrowed. With an LTV of 90 percent, however, the owners would owe $180,000 on the property, making the risk much higher.

One of the best ways to determine which options are viable for distressed homeowners is to examine their LTV. The lower the LTV, the more attractive the options:

- **Low:** With a low LTV, homeowners have substantial equity in the property and have three attractive options — cash buy (sell the house to you), refinance, or list the property and sell it to cash out their equity.

- **Marginal:** With an LTV in the mid-range, refinancing or listing the property are the two best options for the homeowners in most cases. If you can work a short sale with one or more lenders, a cash buy may be feasible.
- **High:** A high LTV indicates that the homeowners have little, no, or negative equity in the property and few attractive options. In such cases, a deed in lieu of foreclosure, a short sale, or selling the house at a loss may be the only options.

Assessing the homeowners' credit health

You may decide to give some homeowners a break if they have a strong credit history leading up to this financial fiasco and if their financial future looks fairly solid. To take the homeowners' credit pulse, answer the Yes/No questions below Homeowner Credit on the deal analysis worksheet:

- **Does homeowner make payments in a timely manner?** Prior to defaulting on the current loan, did the homeowners generally make their payments on time?
- **Does homeowner have some bad credit?** If the homeowner is in foreclosure, he has some bad credit, but you can order a credit report to see details. Sometimes, a homeowner has bad credit due to a temporary job loss, but has a new job now that makes them a low-risk borrower, although it doesn't say so on paper.
- **Any judgments, collections, tax liens on credit report?** Assist the homeowners in obtaining their free credit reports, as explained in Chapter 5, and inspect the reports for any warning signs.
- **Any bankruptcy?** Bankruptcy filings in the past are often an indication of future problems.
- **Was bad credit a one-time problem?** If this bad credit was a one-time problem, and the homeowners have a fairly stable income, they may represent a fairly low credit risk.

The answers to these questions help you paint a financial portrait of the homeowners to assist you in determining the types of options you want to offer them. If the homeowners have a terrible credit history and not much promise of future income, you probably don't want to set them up with a lease-option contract or rental agreement, because that's like to set up them and you for future failure. If, however, the homeowners have experienced a temporary financial setback and have the resources in place to recover their footing, you may want to help them regain their footing.

Gauging the homeowners' wants

The homeowners own the property and the problem, so the decision of what to do is ultimately theirs to make. Always ask the homeowners what they want to do. Do they want to keep the home, sell it, relocate? Can they afford the current payments if the lender would be willing to make some arrangements on paying back the past due amounts? Could they afford a lesser payment?

Although what the homeowners want is often unrealistic, ask the questions and jot down the answers so you know. You may not be able to deliver what they want, but with a little creativity, you may be able to get pretty close.

Determining the homeowners' gross monthly income

One last key piece of information you need to complete the homeowners' financial portrait is the homeowner status. This consists of three pieces of information:

- **Employment:** Is at least one homeowner employed?
- **Gross monthly income:** What is the total gross monthly income of the homeowners? (Include "side jobs" if they regularly make extra money working on the side.)
- **Marriage/divorce status:** If the homeowners are currently married, are they going through a divorce?

You don't want to get into a situation with the homeowners in which you're offering them a lease option agreement or renting them the house if they have no income to pay you or if they're going through a messy divorce that's almost certain to wreck their finances.

Assessing the Homeowners' Options

Based on the information in the deal analysis worksheet, you can develop a pretty clear idea of which options are available to the homeowners. In Chapter 9, I describe these options in detail. Here, I list the options again and provide guidelines on which options are best, based on the homeowners' situation and resources:

- **Reinstating the loan:** For homeowners who owe relatively little and can obtain financial help from family and friends, this is the best option. The homeowners don't have to move and usually retain the same mortgage with the same interest rate; although they may have to pay some late fees and attorney fees. Homeowners are often reluctant to seek assistance from even very close friends and relatives. In Chapter 9, I offer some tips on how to encourage them to ask for help.
- **Negotiating with the lenders for a forbearance:** Again, if the homeowners have a fairly solid financial future, the lender may agree to a forbearance and provide a payment schedule that's suitable for the homeowners. Make sure the homeowners agree to a payment schedule they can afford, because they won't get a second chance. Also everything needs to be in writing, and the homeowners must understand everything they're agreeing to.
- **Listing the property:** When the homeowners can't afford the mortgage payments and probably won't be able to afford the mortgage payments in the near future, then selling the property is usually the most prudent option. This is only an option if the homeowners have sufficient time to list, sell, and close. If they run out of time, they may lose a pending sale, their house, and any equity they have built up in it. Time is of the essence.
- **Refinancing the mortgage:** Homeowners who have substantial equity built up in their property may be able to refinance their way out of foreclosure by taking out a mortgage to consolidate their outstanding debt. Calculate the homeowners' totally monthly payments. If they can pay off all of their debt with a new mortgage that requires a lower total monthly payment, they may be able to keep their home. The problem with this option is that usually by the time the homeowner trys to initiate something, their payment history is downgraded to "slow pay" at best, and they may have other issues with their credit history, so they can almost count on a higher interest rate. Make sure the homeowners can afford the higher payment — most cannot.
- **Selling short:** When homeowners have insufficient equity built up in a property, they probably face a situation in which they simply lose the home and have no money to move on. If you can negotiate a short sale by convincing the lenders to accept less than full payment, you may be able to work a deal in which you can pay the homeonwers a little extra for the house and save enough money by paying off the reduced loan amounts to make the deal profitable for you.
- **Accepting your cash offer:** Cash offers are often best if the LTV is low, the homeowners have little time to market and sell the property, and the home requires some major repairs or renovations to make it marketable.

- **Opting for a lease-option agreement:** The homeowner sells you the house, and then you sell the house back to the homeowner on a rent-to-own basis. See Chapter 19 for details.
- **Selling the home and renting it back:** If the homeowners have sufficient income to pay rent, you may consider renting the home to them after you buy it. Chapter 19 covers this option in more detail.
- **Giving a deed in lieu of foreclosure:** Negative equity is a pretty good sign that the homeowners may benefit by offering the lender a deed in lieu of foreclosure. The lender, however, may refuse the offer.
- **Filing for bankruptcy:** Bankruptcy is rarely a good option. It ruins the homeowners' credit and simply delays the inevitable. However, if the homeowners choose this option, check the Bankruptcy box, recommend a good bankruptcy attorney, thank the homeowners for their time, and let them know that you're interested in purchasing the property if they decide to sell it later. Keep in touch with the bankruptcy attorney — you may be able to purchase the property later.
- **Nothing/Pass:** If the homeowners choose to do nothing or you can come up with no creative way to assist them, check the Nothing/Pass box and move on. Keep tracking the property just in case anything changes or the home goes to auction.

Have the homeowners sign and date the Deal Analysis Worksheet at the very bottom stating that they have read and understand the options described.

TIP

Consider creating an audio recording of your conversation. Ask the homeowners whether recording the conversation would be okay in order to protect their interests and yours from any future confusion over who said what. Make sure the recording states the names of all those present and that they are aware the conversation is being recorded. State the date and time of the recording, and then set the recorder on the table and converse naturally.

Presenting Your Offer: The Purchase Agreement

Whenever you buy a home directly from the homeowners, you must present out the terms and conditions of the sale and transfer of the property from the seller to the buyer.

Purchase agreements are fairly standard documents, but they vary from one area to another. Ask your real estate agent or attorney for a copy of the purchase agreement used in your area.

With the assistance of your real estate attorney, prepare and present the purchase agreement to the homeowners. Your area may have special laws governing the sale of property during the foreclosure process, so be sure your attorney checks the agreement and reviews any special issues you need to be aware of.

Your purchase agreement should including the following details:

- Purchase price you are offering.
- Statement that the homeowners are aware that they agree to sell the property below market value.
- Conditional clause, commonly referred to as a *weasel clause,* that provides you with an exit if something goes wrong. A good condition to add is “Sale is conditional upon review and approval of my attorney.” (Most purchase agreements have conditions built in to them, such as “sale is conditional upon home passing inspection.”)
- Date of possession — the date the current residents and their possessions are to move out and you can start working on the property.
- A list of anything in the home not nailed down that is to stay with the property, such as appliances, furniture, or furnishings.
- The agreed-upon condition of the property when transferred to you. You may indicate “current condition or better” or “broom clean.”
- A statement that the buyer is responsible for all closing costs.
- A statement that the seller shall deed the property to the buyer.
- A statement that the buyer may resell the property.
- Amount of earnest money deposit, if any. To prove that you’re serious about the purchase, provide an earnest money deposit to be held by your attorney or the title company and to be released on condition of a successful closing. (Sometimes you need to give some cash to the homeowner, because they are really strapped — keep that amount as small as possible, because any money you give to the homeowner is at risk.)

TIP

Normally, I recommend a fairly substantial EMD (earnest money deposit) when making an offer on a property you really want to show the sellers that you’re serious and you have the money to close the deal — something other buyers may not have. In the case of buying foreclosure properties directly from homeowners, the EMD doesn’t carry much weight if nobody else is presenting an offer — $1,000 is usually sufficient. If an agent is representing the homeowners, the EMD can range from 3–10 percent.

Consider adding a penalty or bonus to the purchase agreement to encourage the current owners to move out on time and leave the property in excellent condition. For example, you may stipulate that $1,000 is to be withheld and paid when the property is vacated in reasonable condition or an extra $500 is to be paid if the homeowners vacate on time and leave the premises broom clean. Be candid and tell them that you will pay the extra money, but only if they do what you both agree on. If they perform, you'll perform. You may even make a check out to them in advance and show it to them — tell them that when they fulfill their end of the bargain, you'll hand over the check. That way, they see you're not stringing them along.

All owners listed on the mortgage must sign the purchase agreement. If a couple owns the property, both the husband and wife must sign the purchase agreement.

If the auction date is fast approaching, you may be able to secure an adjournment by presenting the attorney who's representing the lender with a signed purchase agreement. This provides the lender with some assurance that the mortgage will be paid in full at closing. During the closing, funds are distributed to the lenders to pay off the loans, and the lenders provide payoff letters — written proof that the loans have been satisfied. Don't be shocked if the attorney still wants to proceed to sale, especially in states with redemption periods. The lender doesn't want to lose time in case your deal doesn't close.

Even if you do have a legally binding purchase agreement with the homeowners, other investors may step in and offer the homeowners a little more money or do something else to convince the homeowners to want to back out of the deal. You can certainly make your case to the homeowners, but if they decide they want to sell to another investor, I recommend that you let them. Trying to legally enforce your purchase agreement against a homeowner in foreclosure who has a better deal on the table doesn't exactly look good in the eyes of the court, even if you've acted on the level.

Closing Time

As soon as you and the homeowners agree on the price, terms, and conditions stated on the purchase agreement, contact your attorney or title company to arrange the closing and set a closing date. Your attorney or closing agent can provide you and the homeowners with the paperwork, so you can review it ahead of time.

On the day of the closing, the property is deeded over to you. You pay the sellers the agreed-upon price (typically in the form of a cashier's check), and you or the homeowners pay off the agreed upon balance of any loans taken out against the property. The title company will collect all the money, pay off the loans (liens), and record the deed in your name.

Always purchase title insurance and hire a title company to handle the closing. This ensures everyone who is owed money is paid, that you're insured if anyone lays claim to the property after closing, and makes sure that the paperwork is properly recorded. If you close without a title company (against my recommendation) don't allow the seller to be the one who pays off the loans after closing.

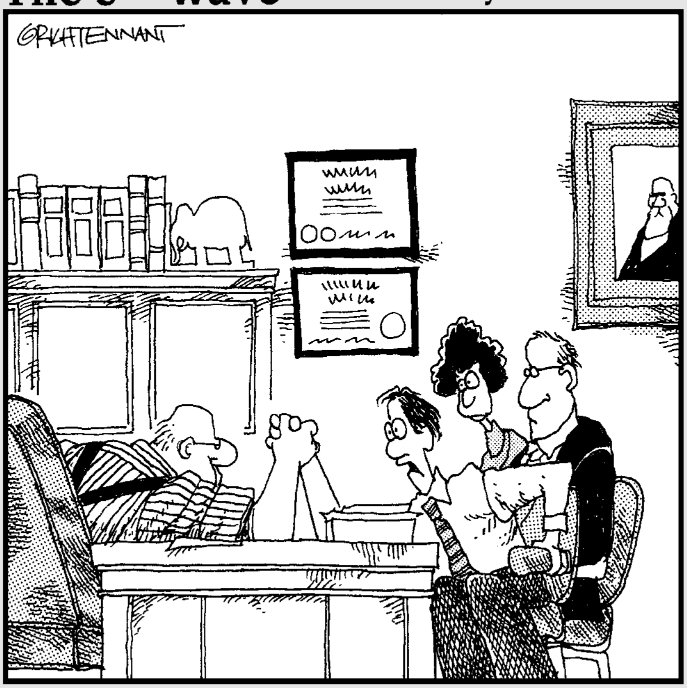
Don't forget to obtain the keys from the sellers. Also, before leaving the closing table, call the utility companies and have the water, electricity, and gas service transferred to your name. Many buyers overlook this important step.

Changing the locks immediately is not a bad idea. You never expect to have a problem, but if you get into some disagreement with the homeowners near the end of the deal, a disgruntled homeowner with an extra key can cause a problem. Protect your investment. Change the locks, but keep the old ones (especially if they're in good shape) — you may be able use them on the next house. I tape the keys to the lockset and put the whole cluster in a safe place, hopefully one you'll remember. The next house I buy, if the lockset matches, I'm ready to go.

Part IV

Finding and Buying Foreclosure and Bankruptcy Properties

The 5th Wave By Rich Tennant



"Sorry, Mr. and Mrs. Benney. As your real estate agent, I wasn't prepared for this kind of negotiation."

In this part . . .

Although stepping into the foreclosure process at the pre-foreclosure stage is usually the optimum strategy, you may be a little uncomfortable dealing with the emotions of distressed homeowners. If the pre-foreclosure stage doesn't interest you, you can find plenty of profitable opportunities during and even after the foreclosure sale.

In this part, I show you how to find and buy properties at auction, from lenders and other institutions that repossess properties or seize them, and from trustees during bankruptcy. I also reveal some additional ways to profit from the foreclosure process without necessarily taking possession of the property.

Chapter 11

Bidding for Properties at a Foreclosure Sale

In This Chapter

- Finding foreclosure auctions
- Calculating your maximum bid amount
- Bidding at open- and sealed-bid auctions
- Tying up the loose ends after the auction

When most people think "foreclosure investing," they think "auction" — a bidding free-for-all where you can purchase properties at bargain-basement prices simply by showing up with a wad of cash. Unfortunately, this is the kind of thinking that gets novice investors into trouble. Without the proper know-how, a knowledge of what you're bidding on, and some self-restraint, you can really get burned at an auction.

In this chapter, I steer you clear of the most common pitfalls and toward the most promising prospects. Here I show you how to properly prepare for a foreclosure sale, so you don't get sucked into a bidding war you're destined to lose. I show you how to calculate and stick to your maximum bid, assist you in packing for auction day, reveal some bidding strategies from a seasoned veteran, and lead you through the process of paying for and holding a property through the redemption period . . . if your area has a redemption period.

REMEMBER

When bidding at a foreclosure sale, keep in mind that you're bidding on mortgages, loans, or tax deeds, not properties. As a beginner, bid only on first mortgages or tax liens, which are less risky investments. When you're more experienced, you can enter into the complex areas of investing in second mortgages or construction liens. Whatever lien position you're bidding on, you should know all the positions, and what owning/holding that position means, so you don't run into problems later.

Tracking Down Auction Dates, Times, and Places

When a lender posts a foreclosure notice or notice of default (NOD), the notice typically specifies the auction date, time, and place. Chapter 8 shows a typical foreclosure notice and highlights the important bits of information it contains. If the place isn't specified, contact the county's register of deeds and ask where the auctions are typically held. In most areas, auctions are held at the courthouse. In some counties, auctions may be held at the property's location.

A couple days prior to the scheduled sale date, call the attorney who's handling the sale and ask the following questions:

- **Is the mortgage going to be auctioned at the advertised date and time?** The sale may be canceled or adjourned if the homeowners filed for bankruptcy or worked out a deal with the lender.
- **What's the opening bid?** The opening bid is the balance of the loan that's in foreclosure plus any interest and penalties. The day before the sale, the attorney should be able to supply you with a fairly accurate amount for the opening bid.

Write this information in the folder you created for the property in Chapter 7.

If the attorney seems reluctant to tell you the opening bid amount, politely let him know that you intend to bid and that your bank needs time to issue a check for the certified funds. Most attorneys will cooperate with serious bidders — after all, their clients (the mortgage companies) need investors to bid on properties. If you win the bid, the next time you call, mention that you bought a property that their firm represented before. This is a huge boost to your credibility. Next time, you won't face such a hassle.

Several days before attending your first auction, contact the sheriff's office or whoever's in charge of handling the auction in your county and find out about what you need to bring to the auction and how the bidding works. The following list gets you up to speed on the basics of what you can expect:

- In some areas, you may need to register ahead of time.
- You need some form of identification, typically a driver's license, but find out for sure.
- The day prior to the auction, call the foreclosing attorney for any of the properties you intend to bid on, find out the opening bid amount, and

head down to your bank to obtain a cashier's check for an amount that exactly matches the opening bid amount.

You need a cashier's check for every property you intend to bid on. If your check is off by a small amount, the sheriff may allow you to make up the difference in cash, but they do not accept large amounts of cash. If you're the successful bidder with an overbid amount of more than one dollar, then you usually have a period of time ranging from one hour to the end of the day to get that amount in. If you win the bid for "plus a dollar," which is one dollar more than opening bid, which means nobody bid against you, have small bills on you to pay that amount immediately.

- Some counties require that you show proof of certified funds either before the sale, at the time you bid, or immediately after the sale.

  Don't bid if you don't have the required certified funds. Not only do you risk losing the property and perhaps getting into some legal mess with the lender and the court, but you could also be banned from future auctions.

- Some counties have minimum bid raises to speed up the process of bidding; for example, after someone bids $1 over the opening bid, subsequent bids may need to be in increments of $100 or $500 higher, or the auctioneer may specify the incremental raise on the fly.

Know exactly what to expect on sale day, so you can remain calm during the bidding process. Some veteran bidders may try to fluster you by asking the auctioneer to verify your funds or ensure that you meet some other requirement. This may seem silly, but if they have the auctioneer question you about something you know nothing about, you may begin to wonder if you're into something that's way over your head, and you may not bid.

Preparing Your Maximum Bid

One of the biggest mistakes you can make at an auction is to start bidding without a concrete ceiling defining just how high you can bid. Set your maximum bid to ensure a 20 percent profit or better, then stick to it. (That means a 20 percent profit on your total investment. It does not mean that you can bid up to 80 percent of the property's value.) In the following sections, I lead you through the process of determining your maximum bid.

Write down your maximum bid in the folder for the property and recommit yourself to that amount before bidding begins. If you think you may be tempted to bid in excess of your upper limit, take someone along with you to act as your conscience and rein you in if your exuberance seems to be overstepping your logic.

Guesstimating the property's improved value

To calculate the maximum amount to bid on a property, start from the end and work back. First, estimate the price you can sell the property for after repairs and renovations. Your real estate agent can provide you with the recent sales prices of comparable homes in the same area. Chapter 10 also offers a discussion on how to estimate the "as is" value of a property that provides useful tips that apply to estimating the improved value of a property, as well.

REMEMBER

When comparing property values, compare apples to apples. Look for homes that have recently sold in the same area that are comparable in lot size, square footage, house style, number of bedrooms and bathrooms, and so on. Don't go out of your way to find comparables that justify a higher bid — that only increases your risk of paying too much for a property.

Estimating repair and renovation costs

From your preliminary inspection of the property, you should have some idea of how much you can expect to pay for repairs and renovations. If you haven't been able to fully inspect the interior of the property, use 10 percent as a ballpark estimate. If, for example, you're buying a property that you are confident you can sell for $150,000 after repairs and renovations, figure in at least $15,000 for repairs and renovations.

WARNING!

When you're purchasing a property at auction, you buy the property in "as is" condition, so you own it no matter how much the repairs and renovations cost. The safest route is to have the house thoroughly inspected, but that's not always possible, so overestimate costs to give yourself a little buffer.

Figuring in holding costs

Holding costs consist of expenses you incur between the time you purchase the property and the time you sell it. Holding costs include the following:

- Property taxes
- Homeowner's insurance

- Interest on any loan you took out to buy the property
- Any utilities you pay
- Recording fee and transfer tax

Water bills, at least in some states, stay with the house. In other words, during the redemption period, while the occupants are running the water, they're also running up a bill that you're likely to get stuck with. If the pipes leak, you pay. Figure this cost into your holding costs.

Add up the monthly amount for each item in the list and multiply by the number of months you plan on holding the property. In an area with a 6-month redemption period, calculate holding costs for the duration of the redemption period plus the number of months you plan to spend on renovations and selling the property.

When I flip properties, I use $100 per day as the average holding costs, but that includes utilities. During the redemption period, you pay only property taxes, homeowner's insurance, and interest if you took out a loan to pay for the property, so your holding costs may be less than $100 per day.

Make sure you know your state's tax foreclosure process and the total taxes owed on the property before you bid. If the tax redemption period runs out during your redemption period and you didn't pay the taxes to protect your investment, the foreclosing bank or mortgage company thanks you for your donation, and you just lost your collateral. Tax liens trump most every other lien, so be aware of any unpaid property taxes.

Subtracting agent commissions and closing costs

I strongly recommend that after you fix up your fixer-upper, you list it with one of the top seller's agents in your market. On average, an agent can sell a home in half the time and for more money than you can sell it for on your own, which not only increases the sale price but also cuts your holding costs. In most areas, the standard real estate commission is 6–8 percent of the sales price, but you may be able to negotiate commissions if you give the agent lots of work.

You're also likely to pay closing costs at the time of the sale. Consult your attorney or title company for an estimate of closing costs.

Arriving at your maximum bid amount

Estimating the future sales price of the property and all expenses related to buying, fixing up, and selling the property is the tough part. Once you have the required numbers, calculating your maximum bid amount comes down to performing some basic math:

1. **Start with the future sales price of the home after improvements.**
2. **For an estimated profit of at least 20 percent, divide the amount from Step 1 by one of the following:**
   - 1.20 in a market where homes values are rising. (To shoot for a 20 percent return on your investment.)
   - 1.25 in a market where home values are steady. (To shoot for a 25 percent return.)
   - 1.30 in a market where home values are declining. (To shoot for a 30 percent return.)
   - 1.35 to 1.50 depending on the percentage profit you want to make. (To shoot for a 35–50 percent return.)

   The resulting number shows you how much you can afford to invest in the property to earn the desired 20 percent return. In a hot market, you shoot for a 20 percent return. In a slower market, you have to aim for a higher return (say 25 percent) in order to hit the goal of making 20 percent.
3. **Subtract any back taxes you will be responsible for paying when you purchase the property.**
4. **Subtract estimated costs for repairs and renovations.**
5. **Subtract monthly holding costs.**
6. **Subtract agent commissions and/or marketing and advertising costs.**
7. **Subtract closing costs for selling the property.**

The result gives you a general idea of how much to offer for the property to be fairly certain you can profit at least 20 percent from the transaction. Check out my site `www.GetFlipping.com`, where I provide a handy Purchase Price Estimator that can do the calculations for you.

Be realistic. Your chances of earning a 40–50 percent profit on a property are very low. You'd have to buy the property for less than 50 cents on the dollar at sale. It's possible. I've done it a couple times, but it's the exception to the rule.

Snagging a diamond in the rough

Your best chance of bagging a deal that gives you a 50 percent or better profit is to do great research and track adjournments. By "track adjournments," I mean keep track of properties that were scheduled to go to sale but had their sales adjourned for some reason or another. Most investors lose interest after the adjournment, leaving some low-hanging fruit that's easy pickins.

Once, I researched a house that sat on a 2.8-acre lot in a very prestigious and highly sought after area in Oakland County. The house was not much to speak of — a smaller ranch style home — but the land was a goldmine. The neighborhood was dotted with multimillion-dollar homes that were all designed by famous architects. Nestled amongst these valuable gems was that little old ranch house — the diamond in the rough. Because of my experience I knew developers would be knocking my door down to get their hands on such a valuable parcel.

I expected very stiff competition at the sale, so I did my homework. When I called the attorney, he informed me that the home wouldn't be going to sale that week. Still, an extraordinarily large crowd showed up at the sale that week all anticipating the bidding to start on this property. When it didn't come up for auction, they all muttered under their breaths and wondered what had just happened.

Fortunately, I knew what happened and what to do about it. I continued to track that property for the better part of six months, calling on it every week to see if it was going to come up for sale that week. Then one week I heard what I had been waiting for — "Yes, actually this will be up for sale, and here is the opening bid." When that woman at the attorney's office gave me that opening bid, my heart started to flutter, and that doesn't happen too much anymore. The reason was that I knew anyone that had been interested in that property had long since given up and forgotten about it.

That morning at sale, I quietly bid the opening bid plus $1.00 and picked up the "diamond in the rough" I'd been waiting for. Those in the audience were stunned. Some thought I had lost my mind and bid on something that I shouldn't have, but there was at least one person I overheard say to their neighbor, "I've been coming here for a while, that was no mistake, he knows something we don't." He was right, my hard work and diligence paid off, and did it ever!

Within a week of the property not being redeemed, I had a rock-solid cash offer for $350,000 from a developer who was going to tear down the house and build another one that would "better fit in with the neighbors." I probably could have held out for more, but you strike while the iron is hot... so I've been told. Oh, by the way I paid just over $150,000 for the property at sale.

Keep tracking the properties after adjournment and continue to bring the property dossier (see Chapter 8) to the auctions with you, so that you'll be prepared if the property becomes available. You may be carrying ten, twenty, or a hundred property dossiers to the auction with you, depending on the size of your market, but at least you won't miss out because you weren't prepared.

The following example shows the maximum bid amount for a $150,000 property in a stable market with $5,000 in unpaid taxes, assuming a 10 percent allowance for repairs and renovations and a 3-month holding period:

Final improved sales price	$150,000.00
Increasing market	dv 1.20
Total	$125,000.00
Unpaid property taxes	– $5,000.00
Repairs and renovations	– $15,000.00
Holding costs	– $9,000.00
Agent commission	– $9,000.00
Closing costs	– $1,500.00
Maximum bid	**$85,500.00**

The opening bid may exceed your maximum bid, in which case, you sit on your hands and either let the bank buy back the mortgage or let some other less informed bidder buy the property and try to wring a profit out of it. If the opening bid is lower than your maximum bid, you have some room to dive in and start bidding.

REMEMBER

This is simply an example to demonstrate how to crunch numbers on a sample property. Not all $150,000 houses are going to fit this model. A house in pristine condition, for example, won't require $15,000 in repairs, and if the taxes have been paid up, you may save a little there, as well, and be able to bid a little higher at auction. Our Purchase Price Estimator at `www.GetFlipping.com` can also be used to calculate a maximum bid amount — check it out.

WARNING!

Make sure you're bidding on a first mortgage and not a second mortgage or some other lien. Many beginners get burned by purchasing a junior lien thinking they're getting a great deal when, in fact, they're paying tens of thousands of dollars for a piece of paper that is likely to be worth nothing after the first mortgage is foreclosed on. You can buy a junior lien to control the senior lien, but that's an advanced move for more experienced investors. See Chapter 19 for details.

Bidding at a Foreclosure Auction

You've done your homework. You inspected the property's title and other paperwork. You visited the property to perform an onsite inspection. Perhaps you even talked with the homeowners and lien holders. You now have a property dossier packed with the information you need to make a well-educated investment decision.

Now, it's show time! Time to pack your briefcase full of your property research and head out to the foreclosure auction for an afternoon of bidding.

Packing for an auction

A couple days prior to auction day, start packing, so just in case you don't have everything you need, you have time to get it. Here's a list of everything you should bring with you on auction day:

- All of the foreclosure property dossiers you assembled in Chapter 7. (Bring all of them, not just the properties you plan to bid on.)
- Paper and two pens or pencils to take notes.
- A calculator.
- A cashier's check for sufficient funds to cover a purchase, if you plan on bidding. Have the check made out to yourself in the amount necessary to cover the opening bid. If you win the bid, you can endorse the check. (In the following sections, I suggest you sit in on a few auctions as an observer before you start actually bidding on properties.)

The bidder and the governor

When you decide to actually start bidding at auctions, consider teaming up with your spouse or someone else you trust. One of you can act as the bidder, while the more restrained member of the team acts as the governor. Over the years I've noticed several couples employ this very strategy.

So, what's a governor? A governor is used to regulate the flow of gas or fuel to an engine, primarily so the engine doesn't get too much gas all at once. During an auction, the governor plays a similar role, restraining the bidder from over-bidding. The bidder remains ready to bid the instant she gets the go-ahead from the governor.

I've seen this technique used as a method to win bids, as well. The governor plays up the role as restrainer, acting as though every bid is inflicting pain, while the bidder is champing at the bit, eager to beat any bid offered by the competition. Just when their competition thinks they've won the bid, the governor gives the nod to bid just one more time. It can be quite a show, but the point is, one or both of the dynamic duo has a maximum bid, and when they pull the plug it's over.

Always be ready to accept losing a bid . . . if winning is going to cost you.

Sitting in on a few auctions

For your first three or four auctions, I suggest you observe and take notes:

- Who's running the sale?
- Who's bidding?
- Who's just watching?
- What are the winning bids on the properties you researched? Jot down the winning bid in the property's dossier.

If someone shows up at one auction and bids on a single property, that person may be an attorney representing the bank. The people who show up every week and bid on properties consistently are foreclosure investors. They're the real deal. These are the people you want to watch, talk with, and learn from.

Wait at least four auctions before you start interacting with anybody. You can say "Hi" exchange the usual pleasantries, but avoid getting into any deep conversations about real estate investing. People who often appear to be know-it-alls and don't actually buy and sell properties can fill your head with all sorts of confusing misinformation.

Crafting a winning bidding strategy

Foreclosure auctions are serious business in which the high bidder stands to acquire a valuable property at well below market value or pay way too much for a worthless piece of paper. It's no board game, and the money's real, so developing an effective bidding strategy is key.

Every bidder has a unique strategy and various techniques for psyching out the competition. Here are some common strategies you may want to try:

- **Bore 'em into submission:** Keep outbidding the highest bidder by the minimum bid. If the minimum increment is $10, whenever someone makes a bid, bid $10 more. Just don't exceed your maximum.
- **Go all in:** Open with an outrageously high bid to shock the competition into silence. This tactic is usually a very bad idea, because it can result in paying thousands of dollars more than necessary. If you're trying to scare off a novice and you know that the property is going to sell for thousands more than the opening bid, you may want to make a dramatic leap, but avoid starting with your maximum bid.
- **Speak softly and carry a big wad of cash:** Quiet bidding often conveys confidence and can undercut the high-energy, emotional tone of the

auction. It forces other bidders to ask, “What did he bid?” which can be a little unsettling and give you the edge you need.

- **Crank the volume:** Bark your bids as if you’re a mad dog in control of the room. If you’ve ever had your parents yell at you, you know the effect this technique can have. It can rattle your opponent just enough to make him back off or make him think that you’ve lost your mind. Either way, you’re in control.
- **Mix it up:** Go erratic, random. Don’t follow a pattern. As long as your bids make sense to you without exceeding your maximum bid, experiment and see what works best.

Submitting sealed bids

Some auctions require buyers to submit their bids in writing in sealed envelopes. Once all the bids are in, they’re opened, and the property goes to the highest bidder. If you’re buying foreclosures in an area that uses sealed bids, you won’t be able to use the clever techniques described in the previous section.

Toying with the competition

I attended an auction where I got into a bidding war with a “bore ’em into submission” bidder and decided to have a little fun with it. The minimum bid was $10. Every time I would bid, my nemesis would bid $10 more. The bidding proceeded like this:

I opened with a bid of $120,000.

Bore ’em countered with $120,010.

I bid $130,000.

Bore ’em bid $130,010.

I bid $135,000.

Bore ’em bid $135,010.

That’s when the fun began.

I bid $139,990.

Bore ’em fidgeted during an awkward moment of silence. The audience caught on to what was happening, and a few people started to laugh. Even the sheriff chuckled a little.

It took Bore ’em about a minute to calculate his next bid: $140,000. He spent another couple minutes trying to figure out what was happening.

At this point, I strayed from the script. With a big smile on my face, I announced, “Ah ha, so you can bid in big round numbers after all!” and then proceeded to bid $140,010, much to the pleasure of the crowd.

Bore ’em was too flustered at this point to continue bidding. I acquired the property in addition to my own personal following. For several weeks after that, the crowd returned just to watch the show.

–Anonymous bidder

Winning a sealed bid hinges on your ability to size up the competition and how confident you are in your maximum bid. If you think the property is going to draw a lot of competition, you may need to submit your maximum bid. If you're fairly certain nobody else is going to bid against you, you may want to submit a dollar more than the opening bid amount.

TIP

If you're constantly losing, you're probably bidding too low. When your bid loses, ask the sheriff or check the public records to find out how much the winner bid. Compare that to your bid and make the necessary adjustments. Keep in mind, however, that a winning bid doesn't always mean the person bid the right amount. The winner may have actually bid too much and will suffer later when the property isn't as profitable as expected.

Following Up . . . After the Auction

You submitted the winning bid. Congratulations, but you're not quite finished. Now, you have to take several steps to pay for the property and protect your interest in it. Proceed through the following checklist to make sure you've attended to all the details:

- **Follow through on the conditions of the sale.** Ask the Register of Deeds or whoever is holding the auction to supply you with a list of conditions to finalize the sale. Read through the conditions and draw up a list of what you have to do. Consult your attorney if you find anything confusing. Once you know what to do, do it.
- **Pay any remaining balance.** If you didn't have to pay the full price you bid immediately following the auction, you have a limited time to pay off the balance — typically less than 30 days, but in some cases you have only a couple days or a couple hours to pay up. Be sure you pay the full amount on time, or you may end up losing the property.
- **Record the deed.** Upon payment or after some period of delay, you receive the deed to the property. As soon as possible, take the deed to the county clerk's office or register of deeds and have it recorded to protect your legal claim to the property. This provides extra insurance to prevent someone from filing another deed and claiming that they actually purchased the property. Some states are "race to record" states, meaning that the first to file the deed obtains the strongest position. Putting off this important step could jeopardize your position. In some counties the sheriff may record the deed.

Ask the Register of Deeds or your real estate attorney to explain the recording requirements in your area. You usually have a grace period from the time you receive the deed to the date on which you must record it, but the recording date could affect the redemption period. In Michigan, you have 21 days to record the deed in order to have the redemption period start from the date of sale. If you miss the deadline, the redemption period may commence sometime after the date of sale.

- **Obtain title insurance.** Visit your title company and obtain title insurance for the property. Using a title company that's familiar with the foreclosure process is best. Check any restrictions (or exceptions) on the title insurance carefully, ask the title company representative to explain any you don't understand, and see if you can have them removed. If your area has a redemption period, the title company may offer a title commitment that takes effect only after the redemption period expires, but this is usually not a problem. Assuming you hold the first lien position and taxes are paid up, when the redemption period expires, other liens will be wiped out and you are going to have full title.
- **Obtain property insurance.** If any major damage occurs to the property during the redemption period, you want to have an insurance to pay for it. Contact your insurance agent as soon as possible to obtain a policy for the home.
- **Notify any taxing authorities who have liens on the property.** If the IRS or the state has an income tax lien on the property, the foreclosing attorney usually notifies the IRS prior to the sale. Make sure the IRS notice accompanies the bidding paperwork. If the foreclosing attorney did not notify a taxing authority who has a lien on the property, consult the foreclosing attorney and your own attorney, if necessary.
- **Return any overbid money to the homeowners.** An *overbid* situation occurs if you bid more than is required to cover any liens on the property. When a buyer submits an overbid, the homeowners have the right to claim the overbid amount. All they have to do is go down to the courthouse, file a claim for the money, and it's theirs.

If someone outbids you at the auction, your area has a redemption period, and you're still interested in buying the property, consider writing a letter to the homeowners informing them of their redemption rights. Figure 11-1 provides a sample letter.

Fruitless labor from a failure to follow through

I purchased the senior lien on a property at an auction and received a sheriff's deed that allowed me to take possession of the property at the end of the six-month redemption period, assuming nobody redeemed my sheriff's deed. I later learned that another investor had stepped in and bought the property directly from the homeowners for about $10,000 to $15,000 cash. Typically when this happens, the investor who purchased from the homeowners redeems the sheriff's deed. In other words, this other investor needed to pay me off before the redemption period expired.

As time passed, I watched the investor as she slowly transformed the house from a run-down shack into a very respectable looking home. I was a little surprised, however, that nobody had contacted me about redeeming my sheriff's deed.

About five months into the redemption period, the house was completed, and a For Sale sign went up in the yard, but I still had not been contacted about a payoff. I got a little nervous and decided to check the title. My sheriff's deed was there plain as day right where it should be. No superior liens had been placed on the property.

The day after the redemption period expired, I took my usual steps and filed for possession. A couple of days later I got a call from a very distraught woman. She explained to me that this was her first investment house and that she had learned how to "flip houses" from a late night "real estate guru" but didn't realize that the deed she obtained was subject to the sheriff's deed, which I held. I told her that what she had done was "lost everything." The phone went silent, and then under a muffled cry she asked, "What do you mean I lost everything?"

"Well," I said, "I now own the house legally per my sheriff's deed, and you have to take down the For Sale sign and stop trying to sell my house." (I was being particularly blunt, so that she would grasp the importance of the situation.) Again, she explained how she had intended to redeem the property, but had failed to do so, and that she had put money into rehab, yada yada yada. I felt really bad for her and the position she was in, so I asked her "What would you do if you were me?"

She said, "I guess you could say 'Thank you very much for a lovely new house,' and then sell it for a profit, but I would like to see us be able to work something out." And that's what we did. I told her that she was definitely going to lose money, and probably a lot of it, but that I would soften the blow by giving her a portion of what she spent on rehab, but that she wouldn't be getting the profits. So, we agreed on a dollar amount, and after selling the property, I paid her the agreed-upon amount. She lost all the money she paid the homeowners plus any profits she expected to see.

Before you write me off as a total jerk, I should explain why I acted like such a "heartless beast." When talking with this particular investor, I learned that her secret to buying properties was to watch me at the sheriff's sale and then approach the owners of the properties I had bid on at auction. She told me that she was so confident in my research that she seldom if ever researched the properties herself — she just piggy-backed on my hard work and efforts.

Well that didn't sit well with me. I don't mind some honest competition, but when you try to take the easy way out, sometimes justice has a funny way of catching up with you. It certainly caught up with her. I consider myself a fairly nice guy, because I turned what could have been a third-degree burn into a harsh and painful sunburn — painful, but not lethal. I heard later through a mutual investor that she had gotten out of the "flipping" game, because once she started doing all the research herself, it didn't seem worth it to her.

This story has two morals to it: Do your own research, and tie up the loose ends.

<Your Address>
<City>, <State> <Zip>
<Date>

<Homeowner's Names>
<Address>
<City>, <State> <Zip>

Dear <Homeowner's First Names>:

I've sent you many letters in the past about the foreclosure process. Unfortunately, those letters went unanswered. This letter is to inform you that your mortgage to <Bank's Name> was sold to <Winning Bidder's Name> at mortgage sale on <Date of Sale>, for <Sale Price>.

By law you have <Number of> months to redeem your property, which means you have until <Redemption Date> to pay off <Winning Bidder's Name> the <Sales Price> plus interest, at <Interest percentage>. At the Sheriff's Department there is an over bid of <Overbid Amount> waiting to be claimed. However, if you choose to pick up this money, you will have a much more difficult time redeeming the property, should you choose to do so. Either way, you may contact <Sheriff Department Contact Person's Name> at the Sheriff's Department at <Sheriff Department's Phone Number> for more information.

The purpose of my letter is to help you either save your home or sell it so you do not lose it in foreclosure. You still have time to act, but time is running out. I may be able to assist you. Please contact me as soon as you receive this letter so I can help you get out of this situation. My number is <Your Phone Number>.

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

Figure 11-1: Inform the homeowners of what happened at the sale and where they stand.

REMEMBER

If you're buying foreclosure properties in an area that has a redemption period, you're not out of the woods yet. Check out Chapter 16 for suggestions and tips on how to survive the redemption period and assist the homeowners in moving on with their lives and out of the house.

Chapter 12

Buying Repos: Bank Foreclosures and REO Properties

In This Chapter

- Getting the lowdown on the REO process
- Networking with REO officers to find the best deals
- Contacting REO brokers for additional leads
- Scheduling your offer for optimum results
- Presenting an attractive offer to the bank's REO officer

When you sit in on a few auctions, you may notice that the opening bid is the final bid. A lucky investor may scoop up a deal uncontested simply by bidding the opening amount plus one dollar. More likely, however, the lender's representative, seeing that no investor is willing to submit the opening bid, buys back the mortgage on behalf of the lender. The lender can then sell the property in an attempt to recoup some of its losses or even turn a profit.

After the lender takes possession of the property, it turns the property over to its REO (Real Estate Owned) division or to an REO broker, who prepares it for resale. As an investor, this provides you with another buying opportunity in the foreclosure process.

This chapter shows you how to approach the lender's REO officer or broker and present an offer that enables the bank to cut its losses while providing you with a valuable investment property.

Acknowledging the Drawbacks of REO Opportunities

You won't always find the best deals in REO properties. Lenders aren't simply willing to give away properties so they won't have to deal with them. Each case is different, and you may discover that REO's are not the best deals in town for any of several reasons, including the following:

- Prior to auction, lenders often ask their local REO broker to provide a BPO (broker's price opinion) or comparative market analysis to determine the current value of the property. Using this information, the lender knows the market value of the property and is unlikely to want to sell below market value.
- The bank may have already written off the debt and may not have to "cut its losses." To the bank, the house may represent a windfall profit, not a burden that it needs to unload.
- Some banks, especially smaller, smarter banks are developing REO departments that are quite capable of rehabbing and selling properties. I have even seen cases in which the bank offers the foreclosed-upon homeowner cash to move out, just as an investor would do.
- Banks are highly motivated to turn a non-performing loan into a profit, and they don't mind unloading their loss on an investor. Be careful. Don't take on the bank's burden if you're not fairly certain you can profit from the property.
- Banks often have several well-established investors they prefer working with. REO departments are often overwhelmed by calls from novice investors making all sorts of promises. They don't have the time to sort through all the calls and determine who's a real investor and who's a wannabe, so they either list with a broker or sell to someone they know.

Although banks and other lending institutions are often in a position of power when dealing with investors, that position can be weakened by pressures from bank regulators. If a bank has too many bad loans on its books, bank regulators begin cranking up the heat, and the bank becomes much more motivated to make deals and cut its losses. You have no way of knowing this, but if you have your financing in place and continue to pursue opportunities, you're more likely to eventually find yourself in the right place at the right time.

REMEMBER

Badgering the loss mitigation or REO department rarely leads to success. In many cases, you won't even get to talk to a person. An automated system simply plays a recording that states the bank's policy and provides you with a fax number. One thing for sure — if you get a break and have the chance to place an offer on a property, you'd better be able to follow through on it. If you waffle, your first opportunity will be your last.

Getting Up to Speed on the REO Process

Banks and other lending institutions (credit unions, mortgage companies, finance companies, and others) like to lend money and collect the interest on loans. They don't like to own property. When homeowners default on a loan, however, and no investor steps in to pay the balance, the lender has no option but to purchase the home, place it back on the market, and try to sell it. Here's how the REO process works:

- When homeowners miss a payment or two, the nonpayment is transferred to the lender's collections department.
- Over the course of 6–8 months, the collections department tries to contact the homeowners to negotiate a payment plan.
- If the collections department is unable to resolve the issue, it transfers the matter to the loss mitigation department, which deals with the problem (and the property) through the foreclosure process. During this time, the lender seeks the assistance of a title company and attorney; the cost for these professionals is added to the *payoff amount* — the total amount required to redeem the property.

When you hear that the house sold for $1 at auction, the house actually sold for the payoff amount plus a dollar. Late-night TV real estate investment gurus spin this fact into a pumped up promise of buying houses for a buck. Don't fall for it.

- At the foreclosure auction, if no investor purchases the mortgage, the lender buys back the mortgage and transfers the matter to its REO department.
- In an area with a mandatory redemption period, the lender's REO department waits for the redemption period to expire, evicts the previous homeowners (if necessary), and sells the property to recover any losses.
- In some cases, especially when the lender is out of state, the lender hires an REO broker to prepare the property for resale and place it back on the market. The REO broker typically gets involved just prior to the end of the redemption period or shortly thereafter. He may play a role in evicting the homeowners or offering cash for keys to encourage the homeowners to move out voluntarily.

At the foreclosure sale, the lender can set an opening bid only high enough to cover the balance of the mortgage and any costs incurred trying to collect that amount prior to the auction. In other words, the lender cannot profit from the sale of the property at auction. When the bank takes possession of the property, however, it becomes the owner and can sell the property for more than what is owed on it. In other words, the bank may not be all that eager to "unload" the property.

Shaking the Bushes for REO Properties

If I haven't yet been able to talk you out of trying to pursue REO properties, you obviously have the determination required to get through to the gatekeepers — the lender's REO people or the broker who's listing the property. Now you have to find these people and present yourself as a reliable investor who can assist them in removing a non-performing loan from their books.

In the following sections, I show you how to properly position yourself as a reliable, trustworthy investor and reveal some strategies for getting yourself connected with the "in" crowd.

Positioning yourself as an attractive investor

Banks and other lending institutions field many calls from would-be investors inquiring about REO properties. A good majority of these investor wannabes have no money. They expect the lender to not only hand them a prime piece of real estate for a bargain price but also finance the purchase and the cost of repairs and renovations. Although some small banks and credit unions may be willing to sell you a bargain property *and* finance your purchase, most larger banks won't even consider it.

REMEMBER

Don't be a time waster. Call an REO officer or broker only if you have sufficient funds to buy, hold, renovate, and sell the property. The best way to succeed at investing in REO properties is to prove yourself — have cash on hand, and do what you say you're going to do.

Hooking up with REO brokers

A good way to find REO properties that a bank is for sure willing to sell is to call on listings with REO brokers — real estate agents who sell properties on behalf of lenders. A good way to track down REO brokers is to network at foreclosure auctions. Start talking with the people who attend these auctions — the *gallery.* They can steer you in the direction of brokers who list REO properties. If that approach doesn't lead you to REO brokers, call on ads that list properties with words and phrases like "REO," "Foreclosure," "Seller Willing To Look At All Offers," and "Bank Owned," or simply call around to local banks and brokers and ask.

REMEMBER

REO brokers are in the business of getting the bank top dollar for the properties they sell, so do your homework. The sheriff's deed filed at the county courthouse after the sale shows what the bank paid for the property. Compare that amount to the listing price to determine if you have room to negotiate. The broker may not cut you a sweet deal, but with proof that you have the financing in place to close the deal quickly and hassle-free, the broker and the bank may be willing to negotiate price.

Getting connected with REO A-listers

When dealing with banks, try to contact the person who's in charge of making the decisions. This may be the bank president, vice president, or someone high up in the REO department. This person can then put you in contact with the lender's REO officer, so when you contact the REO officer, you're making a warm call instead of a cold call. Establishing relationships with bankers requires some people skills and determination that no book can help you develop. Learn by doing and by talking with people.

Consider contacting the banks in your area that have REO properties and let them know what you do. Figure 12-1 provides you with a sample letter of introduction that you can customize to fit your needs.

The exclusive REO insiders club

In the real estate investment community, the REO people often form their own little exclusive club. REO officers may pass along leads for the best properties to their friends, relatives, and other well-connected individuals. REO brokers (who list the properties for the banks) have been known to omit certain properties from the public MLS (Multiple Listing Service), so they can privately offer the properties to their clients of choice.

None of these practices is ethical, and some of them are even illegal, but as an investor, you should know the way the game is played. You may legitimately get yourself on the A-list of investors, but that usually requires hard work, dedication, and a willingness to purchase some less appealing properties for access to better deals in the future.

Remember that no profit is worth what you have to go through if you get caught up in mortgage fraud, or insider deals. Just because "everyone is doing it" and nobody's been caught doesn't mean that you won't be the one the federal authorities decide to make an example out of. Play the game above board; you'll sleep better that way.

<Your Name>
<Your Address>
<City>, <State> <Zip>
<Date>

<REO Manager's Name>
<Company>
<Address>
<City>, <State> <Zip>

Dear Mr./Ms. <Last Name>:

You know better than anyone that the primary business of <Bank's Name> is lending money, not owning property. That is why I want to propose a partnership that I believe will create a win-win situation for both of us.

I'm sure your REO list is full of properties that gobble up your department's valuable time and resources. I'm also sure that you and your staff have more important things to do than worry about property taxes, maintenance expenses, mandatory waiting periods, and all of the myriad other headaches that come with bank-owned real estate.

On the other hand, buying, selling, and owning property is my business. I have the resources to pay cash for properties and the know-how to make them profitable for everyone. Each piece of real estate <Bank's Name> owns represents valuable resources that could be better spent elsewhere in your institution's operations. I would like to help free up that money so you can put it back to work for you.

Let's meet face-to-face to discuss how we can work together in a mutually beneficial relationship. I will call you soon to select a time and date that fits into your schedule. Thank you for your time and interest.

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

Figure 12-1: Introduce yourself to the bank's REO officer via a letter.

TIP

Developing a positive rapport with local bankers and REO personnel is a good move no matter where in the foreclosure process you decide to invest. In many cases, you can establish these contacts when working with homeowners prior to auction. If bankers know that you're working in the area to help homeowners catch up on their mortgage payments, bankers are more likely to respond to you when you approach them about REO properties. In addition, knowing the bankers and other lenders in the area can help you negotiate better deals for distressed homeowners. Get to know the key personnel:

- Bankers, including the president and vice president of the bank
- The manager in charge of collecting late mortgage payments

- The manager of the loss mitigation or REJ (real estate in judgment) department, who handles the property during the foreclosure process
- The REO officer
- The REO brokers in your area

If you're interested in a particular property that the lender is foreclosing on, consider sending the letter shown in Figure 12-2, instead. This letter has a more targeted appeal. In addition, it lets the lender know that you may be able to assist distressed homeowners work out a payment solution — something lenders like to hear. If the lender already turned the matter over to an attorney, you may not get a response. Try sending a copy of the letter to the attorney, as well.

TIP

Create a database or address book for the REO officers and brokers in your area and maintain contact with them. This is an important part of networking your way to foreclosure success, as discussed in Chapter 7.

<Your Name>
<Your Address>
<City>, <State> <Zip>
<Date>

<REO Manager's Name>
<Company>
<Address>
<City>, <State> <Zip>

Dear Mr./Ms. <Last Name>:

I noticed that you had a property go to mortgage sale in <County Name>. This is an area in which I specialize. I would like to see if you have a list of properties that I could purchase in this area.

I also encourage and assist homeowners who are facing foreclosure work with their lenders to develop solutions that are mutually beneficial for the homeowners and their lenders. If one of your customers is behind on mortgage payments, feel free to pass along my name and contact information to the homeowner. I may be able to help.

Please contact me on my direct line <Your Phone Number>.

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

Figure 13-2: Send a letter to the REO officer to inquire about a particular property.

Tracking the property through the REO stage

In Chapter 8, I suggest that you track a property from the time the foreclosure notice or Notice of Default appears until the time somebody eventually purchases the property. If you followed my advice, then you know, from sitting in on the auction, whether somebody purchased the property, but you may not know who purchased it. In many cases, the purchaser is the lender who foreclosed on the property.

To find out who purchased the property, head back to the register of deeds or county clerk's office and check out the deed. Whenever someone buys a mortgage at auction, the first thing he does is record the sheriff's deed he acquired. That deed tells you who bought the property. If the lender bought it, you now know that you have an opportunity to purchase the property from the lender.

Some third-party purchasers intentionally wait to record the deed, so another investor doesn't "poach" their purchase, as discussed in Chapter 12. If you know somebody purchased the property, but you can't find the sheriff's deed with the buyer's name on it, this is probably what's going on. Ask the register of deeds if it has a statutory recording period or deadline of when the deed must be recorded. In some jurisdictions, the buyer must record an *affidavit of designee* or a *buyer's affidavit* — a separate sheet that must be attached to or recorded at the same time as the deed, which tells you when the sale took place, who foreclosed, and more importantly who purchased the property or who needs to be paid off to redeem the property, including their contact information.

Working your way to the better deals

People who work in the REO departments tend to give the best deals to investors whom they trust the most and who offer the best service to the bank. By doing what you say you're going to do, closing on deals, and relieving the bank of its burden, you become an attractive investor. When a property becomes available, the REO officer is more likely to contact you than a less qualified or unproven investor.

You can make yourself even more valuable to the REO department by putting the following tips into practice:

- **Be courteous.** Act like a partner. The bank doesn't owe you anything. Be polite and treat everyone from the bank president down to the secretaries with respect.

- **Solve problems.** When a bank takes possession of a property, it has a problem that you can solve by buying the property. Don't create more problems or provide a litany of complaints. Solve the bank's problem.
- **Take the bad with the good.** REO departments often have some highly profitable properties and some not-so-profitable properties. Offer to buy one property that has a low potential profit along with a property that has a higher potential profit. In other words, bundle your purchases.

When you're just getting started, avoid bundle purchases. I strongly recommend that you purchase properties that are almost certain to deliver a profit. When you become more experienced and have a reliable team that can quickly and affordably renovate several properties at once, bundling may be a good strategy. As long as your overall profit on the bundle is sufficient, you can afford to buy a few mediocre properties along with those that have a higher profit potential.

Following up with homeowners during redemption

In areas with a redemption period, you can continue to work with the homeowners during redemption, even if the bank's REO department bought back the mortgage. Use this opportunity to inform the homeowners that they can still redeem the property.

At this point, the bank isn't likely to reinstate the loan or agree to a forbearance, but the bank may agree to a short sale (accepting less than full payment of the loan's balance). The redemption period also gives the homeowners extra time to find a less painful exit, such as selling the house to you, borrowing from friends or relatives, refinancing, and so on. See Chapter 10 for a complete list of options that may be available to the homeowners.

Another great place to research bank-owned properties is HurryHome.com at `www.HurryHome.com`. This site also enables you to search for preforeclosure and foreclosure properties.

Inspecting the Property

Even when you're buying bank-owned properties, you need to inspect the property with your own two eyes, as discussed in Chapter 9. Getting inside to take a look around, however, can be a monumental challenge. Here are a few suggestions to assist you in inspecting the property as closely as possible.

- **If the homeowners are residing in the home, knock on the door.** They may not let you in, but try to engage them in a conversation long enough to look past them into the house. This doesn't provide you with a thorough inspection, but it's better than nothing.
- **Look through the windows if the house is vacant.**
- **Contact the bank's REO department and explain that you're seriously interested in buying the property but you can't place an offer until you can get inside the house to look around.** Explain that you want to be fair to them, but you also need to know what you're getting into.
- **Offer to visit the house and change the locks for the bank.** Here is a chance for you to problem-solve for the bank. If you have some old locks left over from a previous property you purchased, you can change the locks at no cost to you and seize the opportunity to inspect the home at the same time. Ask them where you can drop off the keys (giving yourself another chance to meet a contact person with some authority).
- **If you can't get inside to take a look around and still want to make an offer on the property, consider adding a contingency clause to the purchase agreement stating that the purchase is conditional upon the home passing inspection.** Remember, however, that contingency clauses make your offer less attractive, but unless the bank flat-out refuses to consider offers with contingency clauses, it's worth a try.

After you inspect the property, follow up with the bank, even if the house is a total wreck. If you like what you saw, place an offer within a reasonable time.

Timing Your Offer for Optimum Results

In real estate investing, being in the right place at the right time often brings you the best properties. This is even more true with REO properties, because banks and other lending institutions are highly motivated to get the bad loans off their books.

As an investor, you have four excellent opportunities to scoop up REO properties:

- Right after the auction, if your area has no redemption period
- Right after the redemption period expires, if your area has a redemption period

- At the end of the month or quarter, when lenders are often in a hurry to clear bad loans off their books
- When the REO broker first lists the property

Banks and other lending institutions often receive funds to lend based on their ration of good-to-bad loans. The more bad loans they can clear off the books, the more money they can invest in potential good loans. In addition, bank officers often receive bonuses and promotions based on their performance numbers, so they're highly motivated, particularly at the end of the month or quarter, to clear those bad loans off the books.

In the following sections, I explore these opportunities in greater detail.

Acting quickly after the auction

If your area has no redemption period and you've been tracking a property that you're interested in buying, contact the REO broker in charge of the property just prior to the auction. Let her know that if nobody purchases the property at the auction, you're interested in it. Of course, if the property has some equity in it, the broker isn't likely to offer you a clear shot at it after the sale. She's more likely to tell you that if you're interested, show up and the sale and bid.

Tell the REO person that you can save her the time and money of evicting the previous homeowners and renovating the property. You can handle that, assuming she's willing to negotiate the sale price.

Timing your move with the redemption period

In areas with a redemption period, the bank isn't going to move on the property until the homeowners have exhausted their final opportunity to redeem the property. Contacting the REO department during the redemption period, however, is always a good idea, just to let the REO officer know that you're interested in the property.

Once the REO department passes the property to the REO broker, the property is typically listed on the open market, and your competition for that property heats up. By letting the REO officer know that you're interested in the property, the manager may tell the broker something like, "Hey, so-and-so really wants this house. I'd like you to hook up with him and get an offer." The letting the officer know of your interest provides you with an opportunity to be the first person to place an offer on the property, assuming the REO officer doesn't already have someone lined up.

Tuning in to the lender's fiscal calendar

Banks often set end-of-month and end-of-quarter dates for their REO personnel. Often, bonuses are tied to an REO officer's ability to unload a certain number of properties in a given time period, and when the end of the month or quarter rolls around, the REO officer is highly motivated to make a deal.

TIP

A bank's fiscal and calendar years may differ, so coordinate your activities with each bank's fiscal calendar. Keep a record of each bank's fiscal year, so you have a better idea of how to time your offers for optimum success.

The crooked broker

In the sidebar earlier in this chapter called "The exclusive REO insiders club," I reveal that the REO circuit is often shady. REO brokers are often in a position of power, and as Lord Acton once said, "Power corrupts, and absolute power corrupts absolutely."

I once had lunch with an REO broker I had known over the years. He wanted to sell me his business. I asked him what I would have to do to guarantee my continued success with his business, and he replied that every once in awhile he sells a house at a good price to the asset manager at a different bank. He would sell them properties that would guarantee a $30,000 profit per property, which is an obviously illegal kickback.

This same REO broker would sell houses to his girlfriend. She would simply buy the property well below market value and then turn around and sell it at market value to earn what's called a *pass through profit.* My staff and private investigating team discovered that the girlfriend had "earned" over $90,000 in pass through profits. That money really belonged to the lender that the REO broker represented.

Another REO broker (scoundrel) I know lists only half the properties he sells. Instead of listing all the properties on the MLS, as he should do, he lists the worst half of them and then sells the listings with the most profit potential to his buddies. We call these *pocket listings,* because the broker puts the listing in his pocket and then transfers it to his friend's pocket. In a matter of days, the listing is sold and closed, and the seller scores a huge profit for doing nothing.

I tell these stories for two reasons. First, don't get involved in these scams. I'm getting the word out about real estate fraud on my site FlippingFrenzy.com, and real estate professionals are joining forces across the country to bust the bad guys. Second, I want you to realize, as an investor, that these sorts of underhanded deals seriously jeopardize your access to the best deals. REO investing isn't easy, and these types of scams make it even more difficult.

Waiting for the broker to list the house

Waiting for the REO broker to list the house is rarely the best move, because the broker's commission is calculated on the sales price of the property. He's not likely to sell you the property at a bargain basement price. Keep in mind, however, that both time and money contribute to making an offer appealing. If the broker can save enough time selling the property to you for less money, he may be willing to broker a deal.

Consider submitting a copy of your offer to the broker and the bank. This isn't necessarily the best way to buddy up with a broker, but it does let the bank know who you are and what you do. In the future, the bank may decide to deal with you directly rather than through the brokers.

Pitching an Attractive Offer

When you're buying a property from a bank or other lending institution, you take the same steps that you would take if you were buying the property from a homeowner. You complete a purchase agreement stating the price and terms you're offering. The bank or other lending institution can and usually does present you with a counter-offer that you can accept or counter on.

In the following sections, I provide some guidance on determining how much to offer for the property and what you can expect when the lender makes a counteroffer.

Banks often require that you sign documents in addition to the purchase agreement that slap more restrictions on the deal. These aren't deal killers, but you should have your attorney look them over before signing them.

Sizing up the lender's needs

When pitching an offer to a seller, knowing what the seller needs can always help. In most cases, the REO officer or broker who's selling the property estimates a target price by totaling the following amounts:

- Unpaid balance on the loan
- Collection fees
- Legal fees and other expenses related to the foreclosure
- Property taxes the bank paid

- Repair and maintenance expenses
- Other expenses

If the home is obviously worth much more than the unpaid balance on the loan, the bank usually takes this into consideration and seeks to profit from the sale in excess of simply recovering the unpaid loan balance and expenses.

Re-evaluating your needs

Knowing how the lender calculates the asking price is valuable information to have when preparing your offer, but more important is knowing the maximum price you can pay for the property in order to be fairly certain that you can resell it for 20 percent more than you invest in it.

In Chapter 12, I provide detailed instructions on gathering the numbers and plugging them into a formula to determine your maximum bid. The formula is the same for determining your top offer on an REO property:

1. **Start with the future sales price of the home after improvements.**
2. **For an estimated profit of at least 20 percent, divide the amount from Step 1 by one of the following:**
   - 1.20 in a market where homes values are rising. (To shoot for a 20 percent return on your investment.)
   - 1.25 in a market where home values are steady. (To shoot for a 25 percent return.)
   - 1.30 in a market where home values are declining. (To shoot for a 30 percent return.)
   - 1.35 to 1.50 depending on the percentage profit you want to make. (To shoot for a 35–50 percent return.)
3. **Subtract any back taxes you will be responsible for paying when you purchase the property.**
4. **Subtract estimated costs for repairs and renovations.**
5. **Subtract monthly holding costs.**
6. **Subtract agent commissions and/or marketing and advertising costs.**
7. **Subtract closing costs for selling the property.**

The result gives you a general idea of how much to offer for the property to be fairly certain you can profit at least 20 percent from the transaction.

Haggling with REO managers

Once you've established a close relationship with an REO manager, you can get away with making your first offer your best offer — as long as the REO manager knows that you've done your homework, can close the deal, and this is truly your best offer. The worst that can happen is that the REO broker rejects your offer.

The worst thing you can do is pitch $200,000 as your best offer and then increase that offer when the broker counters it. I was once trying to sell a house to a couple with whom I was unwilling to haggle (not in the mood, I guess). I told the buyers, "Give me your best offer. If it works, we'll go with it. If not, then I'll tell you that up front too." I needed $150,000 to make the deal work for me. They offered $135,000, and I said, "No, that won't work." They immediately upped their offer to $145,000, and I said, "I thought $135,000 was your best offer. Didn't I tell you that I would be willing to deal with you if you gave me your best offer?" The buyers replied, "Well, yes, but . . ."

At this point, the buyers' credibility was in shreds. I offered to sell them the house for $157,000, saying, "And this IS my final offer." The couple bought the house.

The take home message is this: If you don't want to haggle, don't haggle. If you have a relationship with a REO manager, and he says "Alright, let's just cut to the chase, and you tell me what you want to pay, and if it works we're a go . . .," and then you low-ball him thinking he'll counter, you've just lost your credibility.

REMEMBER

Don't make your first offer your best offer. REO officers are trained to haggle, and they always counteroffer. If you want a property for $200,000, and you offer $200,000, the REO officer is going to counter with $220,000 or $225,000. To get the property for $200,000, you'd better start with a lowball offer of $175,000 or $180,000. This is pretty much a hard-and-fast rule, but be prepared to take a different strategy if the situation warrants it, as I demonstrate in the following sidebar, "Haggling with REO managers."

Drawing up an offer in writing

Whether you're buying a property from homeowners or from a lender, your offer must be in writing — in the form of a *purchase agreement.* In real estate, verbal agreements and handshakes are not enforceable and won't hold up in court. Everything must be in writing. Your attorney can assist you in drawing up and presenting the purchase agreement. Even if someone tells you a price she's willing to accept, get it in writing. Follow the rules to meet the statute of frauds, and your offer will go from an unenforceable oral offer, to a rock solid legally enforceable one.

TIP

When pitching an offer to a bank, you typically have to offer a few more concessions than when you're buying a property from a homeowner. Following are some guidelines to assist you in drawing up an attractive offer:

- **Cash is king:** Having the cash available enables you to close on the deal without having to wait for loan approval. This gives the bank confidence that you won't back out on the deal at the last minute, and it gives your offer an edge over any other offers the bank may receive. Gather proof that you have the cash — copies of bank statements (with account numbers blacked out) and other financial statements.
- **Proof of financing:** If you don't have cash, you need proof that you are pre-approved for a loan. Contact your lender to obtain the required documentation.
- **Large down payment:** If you can't come up with all the cash, offering a large down payment is the next best thing. A 20 percent or higher down payment along with a pre-approval letter from the bank or investor who's lending you the money usually carries sufficient weight.
- **Bank's purchase agreement:** You may be required to use the bank's purchase agreement to present your offer. Banks often do this, so their employees can easily locate the necessary information on a standard form rather than having to learn how to read various purchase agreements.
- **No conditions:** When buying a property from a homeowner, you often make your offer conditional upon the house passing inspection. When buying from a bank's REO department, any conditions weaken your offer, and the bank is likely to reject them outright.
- **Bank's addendum:** The bank typically counters with an addendum of its own stating that the purchase is unconditional, that the bank provides no warranty for the property, and so on. These addendums basically state that you're agreeing to buy the property "as is," which can be a little intimidating, but that's part of doing business with the bank's REO department.

TIP

Prepare all the documentation well in advance and have your attorney review it before signing. Your attorney can do little to help you after you've signed.

After you and the lender agree on a price and terms, have the lender work with your attorney to set a closing date and review any documents prior to closing. At this point, the closing arrangements are pretty much in the hands of the bank and your attorney. The closing is typically held within 10 to 14 days providing there are no other timing issues that need to be met.

During negotiations, never counter yourself. After making an offer, wait for the bank to accept your offer or counter back. If you offer $160,000 and then begin to think that your offer is too low and boost your offer to $170,000 before the bank has responded, you end up bidding against yourself. On the other hand, if you have reliable information and know that the bank has multiple offers, you may want to increase your bid.

Closing on the deal

Even when you're purchasing a property from the bank, always purchase title insurance. You can get seriously burned if you missed something on the title work or a lien was not properly recorded against the property and you don't have title insurance.

During one transaction, I entertained the idea of foregoing title insurance and saving a little money. The deal seemed pretty straightforward, and I had done my research, so I figured I had covered all the bases. I decided, however, to live by my rule, and I scheduled the closing with a title company. Good thing I did.

The closing went smoothly enough — no problems. Weeks after the closing, however, I started receiving notices of taxes and fees I supposedly owed on the property. First, I received a notice from the county treasurer that I owed a fairly substantial amount in back taxes. Then, one of the condominium association's board members stopped me to say that I owed some back dues. The board had just voted to file a lien against my property. In both cases, I thought there must be some kind of mistake, because I had just closed and everything was paid at that closing, or so I thought.

Had I not purchased title insurance and had the title company not handled the closing, I would have had to pony up thousands of dollars extra to keep my property. As it turned out, the title company was responsible for paying, because it made the mistake. The moral of the story? Always use a title company to insure the transaction.

Chapter 13

Finding and Buying Government Repos

In This Chapter

- Finding and buying HUD homes
- Tracking down VA properties
- Buying a bank's assets when it goes belly up
- Finding and buying government-owned and -seized properties
- Qualifying for government financing

The government often plays a supporting role in the real estate business. It insures or secures loans, and when homeowners default on those loans, the government has to step in, foreclose on the property and then sell it to recover some or all of its loss. When citizens fail to pay their taxes, the government may seize the homeowner's real estate to cover the bill. Law enforcement agencies often get in the act by seizing homes of convicted drug dealers and other criminals.

Nobody likes to think of the government kicking people out of their homes, but that's a tragic reality that some homeowners face when they experience a significant financial setback, commit a serious crime, or make some poor financial decisions.

Anyone with enough money or financing can purchase these homes, either from designated real estate agents or by bidding on the properties at auction. In this chapter, I discuss the pros and cons of buying government-owned properties and show you how to track them down, online and off.

REMEMBER

Strictly speaking, the properties I cover in this chapter are not your average foreclosure properties, but because they're properties that are taken away from the owners and then placed on the market, I lump them in with foreclosures.

Why is the government in the real estate business, anyway?

Homeownership is one of the major forces that drives local, state, national, and even global economies. In addition to providing people with a roof over their heads, a home is one of the best and most accessible investment vehicles for the average citizen. It's no wonder, then, that the federal government goes out of its way to facilitate the purchase of homes by making home loans more affordable, especially to first-time buyers.

For decades, people have relied on FHA (Federal Housing Authority)-insured loans to finance the purchase of their first homes. Likewise, veterans have used federally guaranteed VA loans to purchase homes. Most government-secured loans are originated by mortgage brokers. At closing or shortly thereafter, the loans are assigned to lenders who service the loans.

Lenders love these loans, because the government takes most of their risk out of the equation by insuring the loans. If the homeowners default on the loan, the lender has a relatively safe exit:

- **HUD Homes:** FHA loans are insured by the federal government program (through HUD). The lender forecloses on the property and then has two options: keep the property or turn it over to HUD and be fully reimbursed for all costs, including principal, interest, late fees, and court and attorney fees. HUD then sells the house.
- **VA Homes:** The VA underwrites the loan, and because the loan is being offered to war military veterans, the VA is a little more lenient with loan qualifications. When homeowners default on a VA loan, the lender forecloses on the property and evicts the homeowners. The lender then assigns the property back to the VA and is reimbursed all costs.

When a homeowner defaults on one of those loans, the government usually ends up with the property, but has neither the means nor the motivation to fix up the home and sell it. These government properties then go back on the market, where investors can often pick them up for prices below market value.

Bargain Hunting for HUD (Housing and Urban Development) Homes

First-time buyers often finance their homes through the federal government, primarily by way of FHA-insured loans. When the property owner fails to make mortgage payments on the property, FHA initiates a foreclosure, which commonly results in the agency taking possession of the house and reselling it through a HUD-registered real estate agent.

In the following sections, I discuss the pros and cons of investing in HUD homes, encourage you to hook up with a HUD-registered real estate agent in your area, and show you how to research HUD homes online.

HUD sells homes "owner occupied." If you purchase a HUD home, you must sign a document stating that you'll live in the home for at least 12 months before selling it. You may be tempted to stretch the truth a bit and sign the document even though you have no intention of living in the house, but that's fraud. If you're caught and convicted, you may face a hefty fine and some jail time. Do the right thing. If you don't plan on living in the house for at least a year, don't buy it. You can find plenty of good deals on investment properties without committing a felony.

Weighing the pros and cons of HUD homes

Because HUD homes are sold "owner occupied," they're not candidates for a quick flip, but as an investor who probably needs a place to live while investing in other properties, a HUD home may be a good long-term investment. Before becoming involved with HUD homes, however, be aware of the following potential drawbacks:

- HUD homes are often sold at market or just below market value, so they're not always the best deals available. You need to assess the potential profitability of these properties as you would any property you consider buying.
- The homes that HUD owns are typically low- to mid-market homes repossessed from first-time homeowners. They're rarely located in the ritziest neighborhoods.
- You need to purchase the home through a HUD-registered real estate agent and pay a sales commission.
- HUD homes are sold as-is, so have the home professionally inspected before making your offer. After you buy it, you own it, my friend . . . and all the defects that come with it.

One of the big benefits of purchasing HUD homes is that you may qualify for FHA financing. The agency often offers special interest rates for loans used to purchase and rehab run-down properties.

Don't just assume that because the government is selling the home you're getting a great deal on a great property. Do your homework. Inspect the house yourself, research comparable property values in the area, and have the home professionally inspected before you hand over your money.

Hooking up with a HUD-approved agent

If you're interested in investing in HUD homes, hook up with a real estate agent who specializes in these properties. The right real estate agent can supply you with a steady stream of leads along with tips on how to best profit from your investment properties.

You can find HUD-approved agents by networking or by checking out HUD homes for sale online, as discussed in the following section. Online listings typically display contact information for the agent who's listing the home. When you contact the HUD-approved agent, tell the agent if you're already working through your own agent; otherwise, you can end up in the middle of a messy legal battle.

TIP

Sales of owner-occupied houses fall through more often than investor deals, so don't give up just because someone "bought" the property you wanted. Keep an eye on the pending sale and be prepared to pounce if the sale falls through. At that point, most of your competition in the property has lost interest and dropped out.

Finding HUD homes online

HUD Homes Listings at `www.hud.gov/offices/hsg/sfh/reo/homes.cfm` enables you to search by state for homes made available through the U.S. Department of Housing and Urban Development. Most listings provide a complete description of the property along with a photo and links to additional information, including disclosures, environmental compliance, and condition of the property. See Figure 13-1.

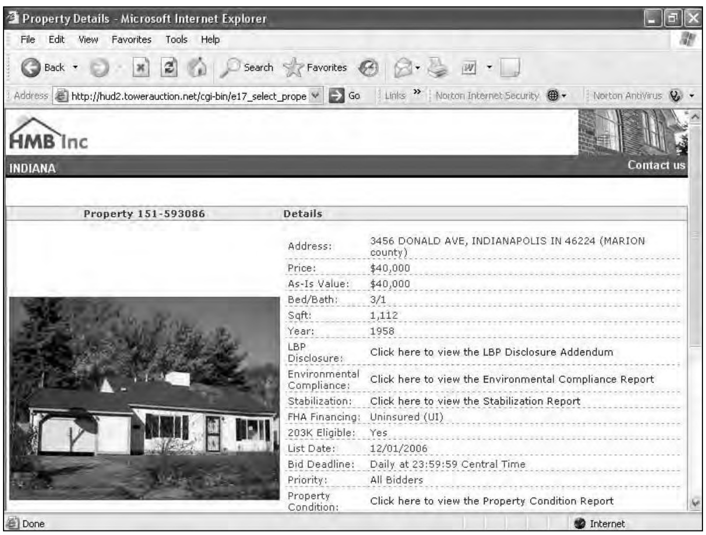


Figure 13-1: Go online to find HUD home listings in your state.

After you find a home, you can place a bid online or click a link to obtain contact information for a HUD-registered broker in your area. In most cases, you have to make an offer through a registered broker.

If someone tries to sell you some HUD-Homes-Investor program for $1,500 or so, don't fall for it. He can't tell you any more than what I revealed here. HUD and VA home opportunities are equally available to anyone who has the financing and energy to pursue them. Don't assume you need some special high-priced program.

Finding and Buying VA Repos

To make homeownership more affordable to military veterans, the U.S. Department of Veterans Affairs (VA) offers VA loans. As you've probably guessed, when someone defaults on a VA loan, the VA repossesses the property and places it back on the market. You can find VA listings in either of the following ways:

- Contact a VA-registered real estate agent in your area.
- Visit Ocwen at `www.ocwen.com`, click Properties for Sale, and click VA Properties. This displays a clickable map of the United States. Click your state and follow the onscreen cues to search for properties in your target area. Figure 13-2 shows a sample listing. You can then contact the listing agent directly or have your agent contact the listing agent to set up a showing.

If you're already working with an agent that you have a relationship with, mention this point when you speak with the agent assigned to sell the VA property. Otherwise, you may inadvertently cause some conflict between the two agents who both want the sales commission, and you don't want to get caught in the middle of some legal battle.

Ocwen is a financial corporation that the VA has contracted to manage its properties. New listings may not yet be assigned to real estate brokers, in which case you can call Ocwen directly to obtain answers to any questions and find out how to present your offer.

You don't have to be a veteran of the military to buy a home off the VA. You may, however, need to sign a statement that you intend to live in the house, just as if you were purchasing a HUD home.

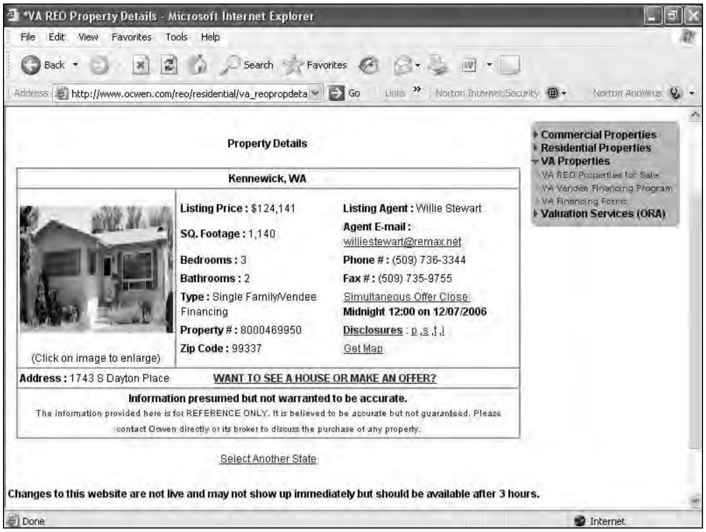


Figure 13-2: Visit Ocwen online to view VA listings.

TIP

While you're at the Ocwen site, click the link for "Vendee Financing" — VA financing that's available for veterans and non-veterans alike. When making your offer, structure it in a way that makes it as easy as possible for the listing agent to say "Yes." Offering a 20 percent down payment streamlines the processing, which almost guarantees instant approval. If you find a really good deal for $100,000, for example, and you offer a down payment of $20,000, you're almost assured of getting the property. The Vendee Financing page has current information about required down payments and fees.

Profiting from Fannie Mae and Freddie Mac Properties

One of the ways the federal government promotes homeownership is by providing financing through Fannie Mae (a nickname for the FNMA or Federal National Mortgage Association), Ginnie Mae (GNMA or Government National Mortgage Association), and Freddie Mac (FHLMC or Federal Home Loan Mortgage Corporation).

All of these organizations do pretty much the same thing — they purchase residential mortgages and then convert the mortgages into securities for sale to investors, indirectly financing the purchase of homes. Because Fannie Mae and Freddie Mac are such an integral part of home financing, they end up with a huge number of foreclosure properties that they must sell, particularly in large markets, and many of these properties are not HUD or VA homes.

If you stumble upon what looks like a great deal, make your offer subject to a satisfactory home inspection. Delaying your offer until you can have the home inspected opens the possibility that another buyer will swoop in and buy the property. By making your offer subject to a satisfactory home inspection, you can get your offer in and then back out if the property needs a lot of work. Present your offer, but make sure it has a good contingency clause you can use for an emergency exit.

Tapping into Freddie Mac's home clearinghouse

Freddie Mac has a Web site devoted exclusively to promoting the sales of the homes it owns called HomeSteps at `www.homesteps.com`. This site features a searchable online database containing information on thousands of homes, primarily REO properties, all across the nation. Freddie Mac lists most of the homes with brokers, but it also holds online auctions, so you can bid for properties in the comfort of your home or office.

To search for homes for sale, simply click Find a Home, click Search for your next home, type the requested information on the search form, and click Search. HomeSteps also has a Home Detective tool that automatically e-mails you a notification when a home that matches your criteria is up for sale. Figure 13-3 shows a sample listing. As you can see, HomeSteps provides very sketchy information about its homes, but it does provide two key pieces of information — the name and phone number of the real estate agent to call. When you find a home that interests you, call the agent to schedule a tour.

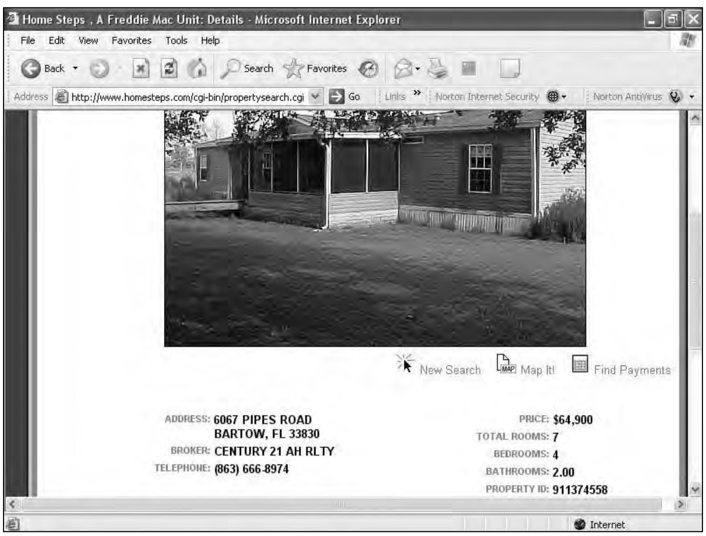


Figure 13-3: HomeSteps can assist you in finding Freddie Mac homes in your area.

Rest your mouse pointer on the Homebuyers tab, which appears on every page of the HomeSteps site, to view a drop-down menu of options for buyers, including Find a Home, Find a Local Agent, Buying a Home, Mortgage Calculator, Getting a Mortgage, Homeowner Promotions, and Auctions. If you don't currently have financing to fuel your investment, click Getting a Mortgage for leads to local lenders. For many homebuyers and investors, HomeSteps offers a complete package for finding a home and securing financing.

Shopping for Fannie Mae properties

Freddie Mac's older sister, Fannie Mae has her own Web site for homebuyers. Go to the Fannie Mae home page at `www.fanniemae.com`, scroll down to the area For Home Buyers & Homeowners, click Resources, and click Fannie Mae-Owned Property Search. Complete the search form to specify your desired price range and location, and click Search.

If Fannie Mae has any properties for sale that match your search criteria, the site displays a list of the available properties, and you can click a link to obtain additional information, including contact information for the listing agent. Figure 13-4 shows a sample listing of a Fannie Mae-owned property. You can also get a map that shows exactly where the property is located.

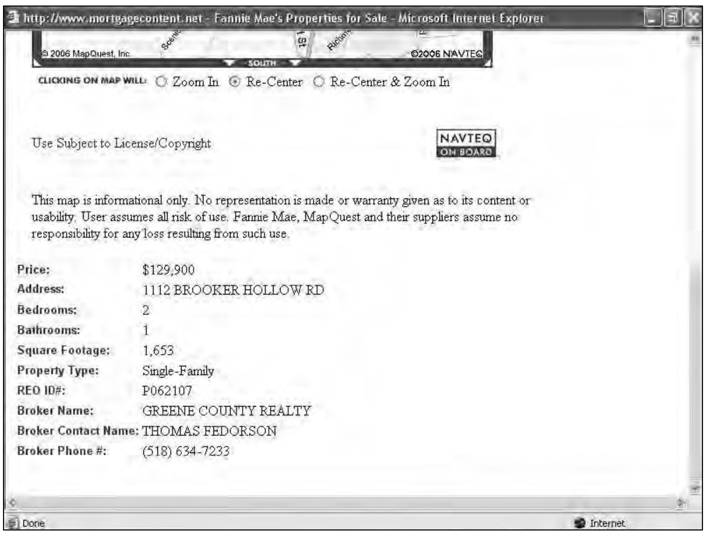


Figure 13-4: Find Fannie Mae homes in your area.

While you're at the Fannie Mae site, check out additional resources for home buyers, including information on lenders and mortgages. If you're an investor who's having trouble finding financing for an investment property, you may be able to finance the purchase through a local lender who's connected with Fannie Mae.

Buying FDIC properties

FDIC (Federal Deposit Insurance Corporation) is a government agency that insures savings deposits at member banks, typically up to $100,000 per savings account. If an FDIC bank fails, the agency makes sure that people who have savings accounts at the bank don't lose their life savings.

When a bank fails, the FDIC acquires any properties the bank owns and puts those properties up for sale. It's sort of like foreclosing on the bank. These properties are then offered for sale. You can check out what the FDIC has to offer by visiting `www.fdic.gov/buying/owned/index.html`, but I wouldn't waste my time. When I visited the site, I did a search for all property types in all states and found three lousy properties for sale somewhere in Texas . . . and they weren't exactly in the heart of Texas.

When a rash of bank failures occurs, you may be able to find plenty of FDIC properties for sale. In the meantime, you can find a wider selection of properties elsewhere. I include this section on FDIC properties only so that you won't think I omitted something by mistake.

Finding and Buying Government-Seized Properties

Various government agencies at all levels often seize or purchase property. None of these agencies is interested in the property itself. They generally want to unload it quickly for whatever they can get for it. In other words, the government is the ultimate motivated seller.

You can track down government-seized properties by contacting law-enforcement and government agencies directly, especially at the state or local level. The following sections describe various agencies — local, state, and federal — that commonly have properties for sale.

House-jacking in Wayne County

Wayne County announced that it was holding the equivalent of the county fair of tax sales. My investment team spent months preparing for it and I actually brought my banker along to the auction. I had the funds on hand to purchase a million dollars' worth of real estate.

I ended up buying only two houses that day — one was a lot without a house and the other was what I would consider a good rental property, perfect for use as a long-term investment. Well, my long-term investment didn't quite turn out as I had planned. I rented it out only to discover later that some sinister con artist had stolen the property from me. I had been victimized by a house-jacker!

That was a little discouraging. After all, I'm a renowned expert on real estate fraud and even have my own Web site called FlippingFrenzy.com, on which I warn people about real estate con artists. I felt like a police officer who just had his squad car hijacked. The perpetrator used the information from the tax sale with the original homeowner's name on it and recorded the deed in his name, before I had a chance to record the deed in my name!

Needless to say, I was able to track down the con artist with the help of my friendly neighborhood law enforcement agency and make him pay for his crime.

The moral of this story is to remain vigilant for real estate con artists, file your deed as soon as possible after the sale, and take out title insurance to cover your back.

Buying properties at tax sales

Taxing authorities don't mess around when citizens don't pay their taxes. They simply send a few notices, and if the homeowners don't come up with the cash or work out a payment plan, the taxing authority seizes on the property, puts it up for auction, and attempts to collect the taxes from the sales proceeds. Taxing authorities show little leniency, and the homeowners rarely dodge the bullet by claiming bankruptcy.

Tax sales, like foreclosures, are typically processed through the county sheriff's office, as explained in the following section, but the state may hold its own tax sales. Your real estate attorney can fill you in on the details and tell you where to go for additional information related to your state and county.

Avoiding the tax lien sales gurus

WARNING!

Most of the tax sales you hear about in real estate investment books, articles, and on late-night TV are property-tax sales. Your average investment guru typically over-hypes the available opportunities in this area. They lead would-be investors into believing that they can pay $4,000 in back taxes at a tax sale and scoop up a $200,000 property. In theory, you may be able to take ownership of a property by paying the back taxes, but in practice, that rarely happens. This area has become so competitive that bidding quickly drives up the price of the property. You would be very lucky to get a $200,000 property for $120,000 at auction.

If you decide to search for "tax sales" or "tax liens" online, even if you look for tax sales specifically in your state or county, you're very unlikely to discover any useful information. You'll find thousands of sites that attempt to sell you on get-rich-quick schemes related to tax sales and purchasing tax liens and very little information directly from official state or county Web sites . . . unless your particular state or county has some good information on the Web (most don't). Don't waste your money on whatever program and services a particular commercial site is peddling. You'll find more valuable information by calling or visiting your county sheriff's office or treasurer's office.

Buying properties from the IRS

In most foreclosure situations, the IRS releases any lien it has on the property. The investor who buys the senior lien must provide the IRS with 30 days' notice, just in case the IRS decides that it wants to redeem the property and try to sell it to recover lost tax revenue, but the IRS usually passes on such deals. Sometimes, however, the IRS takes possession of the property and sells it at auction.

To find out about properties that the IRS has for sale and obtain more information about upcoming auctions, visit `wwww.treas.gov/auctions/irs/`, scroll down the page, and click Real Estate. If you see a property that looks interesting, click its link to view a description of it along with information on the date, time, and location of the sale; encumbrances against the property; contact information about the person in charge of disbursing the property; and a link to a form for mailing in your bid.

Assuming you submit the winning bid, you typically have to come up with about 20 percent of the purchase price immediately for a down payment, and the remainder is due within 30 days of purchase. The homeowners have 120 days to redeem the property, but check to make sure, just in case the IRS changes its rules.

Before placing a bid, inspect the property with your own two eyes and research the title, just as you would do prior to making an offer on any home. The IRS site lists encumbrances against the property, but it may have additional liens that the IRS doesn't know about.

Contacting your county treasurer's office

Your county treasurer's office or property tax division is the best place to start your search for information about tax sales, particularly property tax sales. Visit the treasurer's office or whichever county office handles the tax sales and try to obtain the following information:

- **Bidder's packet:** Many counties put together a bidder's packet with general information for investors. For a small fee, you can obtain most of the basic information you need about tax sales in your county.
- **Property list:** As the date nears for the property tax sale, the county treasurer may offer a list of all the properties that will be auctioned. The problem with such a list is that it's generally a list in progress up until the date of the sale.
- **Regulations:** If your bidder's packet does not contain information about how redemptions are handled for property tax sales, ask. Different states and counties may handle this differently. During the writing of this book, Michigan's tax sales gave homeowners no redemption rights. Once you purchase a property at a tax sale, the homeowners have no chance to redeem it. Find out the rules that govern tax sales in your county.

REMEMBER

The rules and regulations regarding tax sales are very complex and vary from state to state. The entire delinquent tax foreclosure process can take anywhere from three to seven years from the time a homeowner stops paying taxes until the time the government takes possession of the property and puts it up for sale. In that time, the taxing authority attempts to contact the homeowners and anyone else who has a lien on the property, giving them the opportunity to pay the back taxes. In most cases, someone who has an interest in the property ponies up the money and takes controlling interest in the property. Contact your real estate attorney to find out more about how tax sales are handled in your area.

Taking a trip to the department of transportation

The department of transportation (DOT) commonly purchases real estate when building or widening roads or making other improvements to the infrastructure. If the property is not destroyed during the construction project, the department of transportation puts it up for sale. Often, you can buy property directly from the DOT or through an auction at a deep discount.

Contact your state department of transportation for leads on properties they may currently have for sale. They may list the property with a particular broker or post notices in specific legal publications. Find out who's in charge, call and introduce yourself as an investor, and ask if they have any properties for sale. In many cases, the properties consist only of land, but occasionally, you find a property that has a house on it.

TIP

Some DOT Web sites list the properties they have for sale online. Oregon's DOT has a special section on its Web site for property management (`www.oregon.gov/ODOT/HWY/PROPMGT/`). Michigan's DOT also provides information about excess properties at `www.michigan.gov/mdot/`. On most DOT Web sites, however, you won't find much about properties for sale, so you have to make phone contact. The U. S. Department of Transportation also ends up owning property after completing construction projects. To track down properties owned by the feds, you have better luck visiting the sites listed in the next section than trying to wade through the USDOT site.

Finding government-seized property online

TIP

You can poke around on the Web to find Web sites of various federal, state, and local agencies that seize and dispose of real estate. Use your favorite search tool to look for "government seized property," "government-seized properties," or "government-seized real estate." Use your imagination to come up with other search phrases, such as your county or state followed by "seized property." Be sure to check out the following sites:

- **Real Estate for Sale from Government Surplus & Foreclosures** at `www.firstgov.gov/shopping/realestate/realestate.shtml`. It features several groups of links for Commercial Buildings and Land, Farms and Ranches, Single Family Homes, and State and Local Government Sales. Follow the trail of links to your desired destination.
- **US Treasure Customs Seizures** at `www.treas.gov/auctions/customs/realprop.html`. This site features a list of properties that the U.S. government has seized and put up for auction online. In most cases, these properties have been seized because they were purchased with drug money or other funds from criminal activity. Discover more about the auction process at this site.
- **USDA Real Estate for Sale** at `www.resales.usda.gov`. This site displays links to single-family or multi-family properties. Simply click the link and follow the trail of maps to your state and county to find out whether any USDA properties are for sale in your neighborhood.
- **Office of Property Disposals** at `propertydisposal.gsa.gov/Property/`. This Web site provides access to information about properties owned and for sale by the federal government, such as land and buildings made available by base closings or federal marshal property seizures.

If you're looking for properties that law enforcement agencies have seized from drug dealers, racketeers, and other criminals, you may not have much luck contacting the law enforcement agencies. They usually prefer to place a lien on the property and collect some money later — when the property is sold or the mortgage is refinanced. Sometimes the mortgage company offers to pay the lien to protect their interest. In the rare case in which law enforcement does take possession of a property, they typically sell it through an auction house or real estate broker.

Chapter 14

Banking on Bankruptcies

In This Chapter

- Getting up to speed on bankruptcy laws
- Picking a strategy that works for you
- Gaining an edge on the competition
- Getting leads on properties in bankruptcy
- Maneuvering when a foreclosure you bought ends up in bankruptcy

When you're focused on foreclosures, you may overlook another foreclosure-related opportunity — bankruptcies. If financially strapped homeowners file for bankruptcy, they shut down the foreclosure process, buy themselves some time to restructure their finances, and buy you some additional time to work your magic.

Dealing in bankruptcies can be even more complicated than trying to acquire a foreclosure property. In most cases, you can't simply deal with the homeowner or bid at an auction. You have to work with the homeowners' attorney or the court-appointed trustee, who is committed to selling the property for fair market value or at least a fairly decent price. Even if you obtain the attorney's or trustee's approval, creditors may oppose the sale of the property in court. To turn a profit with bankruptcies, you really need to know your stuff.

This chapter delivers tips and tricks to improve your odds of success and shows you what to do when a property you purchased in foreclosure ends up in bankruptcy court.

Acquiring bankruptcy properties can be a royal pain, which is exactly why most real estate investors avoid them like the plague. If you're a novice investor, I suggest you do the same. Because so many investors steer clear of properties in bankruptcy, however, the opportunities are more plentiful for anyone who can learn the ropes. Just make sure you have an attorney who specializes in bankruptcy in your corner.

Brushing Up on Bankruptcy Laws

Filing for bankruptcy is like pressing the Pause button on your DVD player. It stops everything . . . or in legal parlance, it *stays* everything. It stops foreclosure (only temporarily). It freezes the bill collectors. It transforms the bankruptcy filer's loose collection of assets into an estate, from which nothing can move until the bankruptcy courts and trustee can resolve disputes.

As an investor, you're frozen, too. You can no longer negotiate with the homeowners. The home becomes part of the estate, which may need to be sold to pay outstanding debts. If you're already in the midst of negotiations, you must include, in your offer, that your offer is subject to the bankruptcy court's or trustee's approval. Small claims court (a district court) has the most power in bankruptcy.

In the following sections, I explain the differences between the two main types of bankruptcy you're likely to encounter — Chapter 7 and Chapter 13. Consult an attorney who specializes in bankruptcy for specific rules that apply to bankruptcies in your area. Pay close attention to any rules governing what you can and cannot do as an investor.

Selling assets through Chapter 7 bankruptcy

Homeowners filing for Chapter 7 bankruptcy hand over control of all of their assets to a court-appointed trustee. The court empowers the trustee to liquidate the assets in order to pay any claims against the estate, including back taxes, unpaid mortgages, and credit card debt.

When you're negotiating for the purchase of a home that's part of a Chapter 7 bankruptcy, you deal with a court-appointed trustee. You may present your offer to the homeowners, but that offer must state that it is subject to the trustee's approval.

Restructuring debt through Chapter 13 bankruptcy

In Chapter 13 bankruptcy, people seek to *restructure* their debt — that's a fancy way of saying that they work out some sort deal with the people to whom they owe money (the *creditors*). Restructuring may include selling some assets, including the bankruptcy filer's home, assuming they own a home.

When you're negotiating for the purchase of a home that's part of a Chapter 13 bankruptcy, you deal with the homeowner's attorney and must present your offer to the attorney.

Knowing When to Purchase

Acquiring bankruptcy properties requires a great deal of patience. When people normally buy a house, they present an offer, the seller responds in a day or two, negotiations proceed for a few days, and then the buyer and seller meet at closing and seal the deal. When you make an offer on a property in bankruptcy, the seller may still be able to negotiate with you, but the sale must be approved by the trustee or the courts. In addition, the trustee must notify all creditors of your offer, and they must sign off on it. In many cases, the creditors object to the sale.

The value of a good attorney

After I purchased a foreclosure property at auction, the homeowner filed for bankruptcy. She had a great attorney. I didn't.

Two courts became involved in the proceedings — the bankruptcy court was dealing with the bankruptcy, while the district court was handling the foreclosure proceedings. Despite the fact that the homeowner had filed for bankruptcy, the district court gave us permission to proceed with the eviction. Shortly after the court-appointed officers showed up at the house to evict the homeowner, the homeowner showed up with her attorney and then proceeded to attack and bite one of the police officers. She was escorted to jail. After her release, she sued everyone involved. The police dropped all charges.

My attorney did a little more research on bankruptcy law and discovered a few additional items he had overlooked. We moved the homeowner's possessions back into her house, and the bankruptcy court called an emergency hearing. The bankruptcy judge ordered the district court judge and the court officer who had been bitten to testify and requested that I testify, as well.

After gathering testimony, the judge handed down his verdict. The homeowner was allowed to live in the house for another six months for free, and I was ordered to pay her $20,000.

I had all the right paperwork, all the right judgments, but the wrong attorney. He was not well versed in bankruptcy. The homeowner, however, had chosen the right attorney, and it made all the difference.

Shop for an attorney the same way you shop for a doctor. A general practitioner is okay for general legal issues, but when you're dealing with bankruptcy, hire a bankruptcy specialist.

Knowing when to purchase a property is often the key to acquiring it. Following are the various stages in the bankruptcy process along with some tips on how to more effectively position yourself at each stage:

- **Prior to the bankruptcy filing:** At this stage, you can present your purchase agreement to the homeowners and deal with them as you would if you were following the standard operating procedure of buying a home. Unfortunately, at this stage, homeowners who are planning to file for bankruptcy are often reluctant to accept anything less than full market value.
- **Debtor in possession stage:** Upon filing for bankruptcy, the homeowners remain in possession of the property and can accept offers and negotiate the sale. The bankruptcy attorney or court-appointed trustee, however, is legally obligated to notify the creditors, and they must approve the sale. At this stage, you're even more unlikely to obtain the property for a price significantly below market value.
- **Liquidation stage:** At the liquidation stage, control of the property is transferred to the trustee. Unless the judge objects, the trustee is in control of the property and chooses the most attractive offer. This is usually the best time to make your move. Although a creditor can object at this point, the trustee has the power to overrule the objection. Of course, the trustee also has the power to reject your offer and hand the property over to one of the creditors. Dealing with the creditors is often your key to acquiring the property at this stage.
- **Post liquidation:** If one of the creditors buys or is given the property during the liquidation stage, you may be able to purchase the property from the creditor. This is another excellent opportunity to purchase the property, especially if you've established a solid relationship with the creditor.

What happens if the homeowners file for bankruptcy after you've purchased the property at auction? The bankruptcy court may now consider you to be a claimant or creditor, and contacting the homeowners at this point may violate the bankruptcy code. Consult a qualified bankruptcy attorney if you find yourself in such a situation. If you're able to work out a deal with the homeowners and you manage to structure the deal in a way that gets you more money than you would otherwise be entitled to, the court may decide that you received a *preference,* which means that you may be required to *disgorge* (pay back) the excess and then some.

WARNING!

Never contact the homeowners before consulting an attorney who's well-versed in bankruptcy law in your area. In some cases, you may be able to work out a deal that's acceptable to both the homeowners and their creditors, but this situation is like tip-toeing through a minefield. If the homeowners perceive you as working on behalf of the lenders to circumvent their bankruptcy protection, they can have you hauled into court, and you're likely to find yourself paying a hefty penalty.

Tracking Down Houses in Bankruptcy

Bankruptcy is not a private affair. As soon as someone files for bankruptcy, the attorney handling the bankruptcy records the bankruptcy filing and posts a notice in the local paper or legal publication. This provides you with several resources to find out about properties in foreclosure:

- Local paper
- County legal news
- Bankruptcy filings at the county courthouse
- Court-appointed bankruptcy trustees
- Personal bankruptcy attorneys

In the following sections, I show you how to tap into these resources for leads on prospective investment properties.

You often obtain some of your best leads on bankruptcy properties by being involved with homeowners during the foreclosure process. Your prior dealings with the homeowners and their lenders give you a significant advantage in the bankruptcy arena, because you know what's going on and already have established relationships with most of the parties who are involved.

As mentioned in the previous section, when dealing with homeowners who've filed for bankruptcy, be particularly careful. Don't represent yourself as something you're not — if you're not an attorney, let the homeowners know that up front. Tell them that you're an investor who may be able to assist them in working out a win-win transaction. If the homeowners even mention bankruptcy, suggest that they seek independent counsel or ask them to sign a waiver that you offered this suggestion and they decided not to purse this option. If the relationship sours later on and the homeowners claim that you advised them against seeking counsel, a signed waiver provides you some valuable legal protection.

Skimming publications for bankruptcy notices

In Chapter 7, I direct your attention to foreclosure listings or NODs (Notices of Default) that appear in local papers or your county's legal news publications. You can find bankruptcy notices in these same publications.

Check the Public Notices section of your local newspaper's classifieds to find listings of bankruptcies that have been filed in your area. Your county's legal news publication should also have a section devoted exclusively to bankruptcy filings.

The bankruptcy notice contains the information you need to get started, including the homeowners' names and the attorney's or trustee's name and contact information.

Researching bankruptcy filings

Whether you're looking for leads on properties in bankruptcy or have found a lead and want more information, head down to the bankruptcy court at your county's courthouse and request to see the recent bankruptcy filings. Examine the documents for the following bits of information:

- Names of the people filing or bankruptcy
- Whether the husband and wife filed jointly
- Whether bankruptcy was filed under Chapter 7 or 13
- The name of the trustee, if a trustee was appointed
- Whether the house is included in the bankruptcy
- The home's stated value, if included in the filing
- How much of the equity can be protected
- The names of any creditors who've been contacted and whether any of the creditors filed an objection at the confirmation hearing
- The acting attorney's name and contact information
- The schedule for proceedings
- If the bankruptcy hasn't been confirmed when the property will be placed back on the foreclosure docket
- Whether or not the lender has moved to lift the stay

TIP

You can subscribe to an online service for access to bankruptcy filings. I use a service called Pacer, which you can find at `pacer.psc.uscourts.gov`.

Networking with the gatekeepers

Personal bankruptcy attorneys and court-appointed trustees are the gatekeepers who protect those who file for bankruptcy from the bill collectors and from anyone who's seeking to benefit from the misfortune of having to file for bankruptcy, and that includes you.

Although these attorneys may function as speed bumps in your pursuit of investment properties, they can also be a valuable asset. They're typically less involved emotionally, making them easier to deal with, and if you show up with the cash necessary to purchase a home and expedite the liquidation process, an attorney may regard you as an ally.

TIP

Get to know the personal bankruptcy attorneys and trustees in your area. Consider sending a letter of introduction to these attorneys, informing them of what you do and explaining your desire to create a mutually beneficial, long-term relationship. Figure 14-1 shows a sample letter.

<Your Name>
<Your Address>
<City>, <State> <Zip>
<Date>

<Bankruptcy Attorney's Name>
<Company>
<Address>
<City>, <State> <Zip>

Dear Mr./Ms. <Last Name>:.

My name is <Your Name>. I am a real estate investor who regularly works with individuals who are facing foreclosure. They often need information about bankruptcy laws and regulations and legal advice about the proper course of action to take.

I believe we can create a win-win situation by working together to help my clients. You would win from the business I could refer to you. I would win because I believe that once you completely understand what I do, you will send referrals to me. And we both win by being kept fully informed about the progress of clients we refer to each other.

For your review, I have enclosed a few letters from people I have helped in the past. Once you have had a chance to look over these materials, I will give you a call to discuss the possibility of building a mutually beneficial relationship.

In the meantime, please give me a call at <Your Phone Number> or email me at <your email address> if you have any questions. I look forward to speaking with you soon.

Sincerely,

<Your Signature>

<Your Name>

Foreclosure Specialist

Figure 14-1: Introduce yourself to the attorneys in your area who deal with bankruptcies.

Dealing with the Gatekeepers

To acquire a property that ends up in bankruptcy court, you have to serve two masters — the bankruptcy attorney or trustee and the homeowners. In bankruptcy, the legal people are your main contacts at this point, but if you were working with the homeowners prior to the date on which they filed for bankruptcy, you can leverage your relationship with them to influence the decisions.

In the following sections, I provide some tips on how to team up effectively with court-appointed trustees, personal bankruptcy attorneys, and homeowners to liquidate assets and perhaps purchase the home.

WARNING!

Don't toss around terms when you're unsure of their meaning. Terms that have an every day meaning to us common-folk may have an entirely different meaning for an attorney. If the attorney thinks you're using the term the same way she uses it, the two of you create a disconnect that may lead to a costly miscommunication. It can also compromise your credibility if the attorney realizes that you really don't know what you're talking about and are simply blowing smoke.

Cooperating with bankruptcy trustees

In deed of trust states, the court appoints a trustee to carry out the liquidation of property, maximize the amount that goes to the creditors, and dismiss as many claims from creditors as possible. In other words, the court passes control of the situation to the trustee and essentially says, "You sort out this mess in a way that's fairly equitable for all parties involved."

REMEMBER

When dealing with a trustee, realize that this person has a court mandate to sell the property for as much money as possible in a relatively short period of time. As an investor, the best approach is to present a fair offer that gives you a sufficient profit and doesn't turn the trustee against you. If your offer is laughable, you not only risk losing this property, but you also jeopardize any future relationship with the trustee.

Teaming up with bankruptcy attorneys

Bankruptcy attorneys serve both their clients and themselves. Most of their clients don't have deep pockets, so the longer the proceedings drag on, the less they earn per hour of their time. This gives you some room to haggle.

Realize, however, that your haggle room varies greatly depending on the attorney's motivation and skill:

- **Self-interested attorney:** Self-interested attorneys are more motivated to serve themselves. These attorneys typically file bankruptcy for anyone who's interested in filing, regardless of whether the homeowners qualify or will benefit from it. These attorneys simply want to make money and may pressure the homeowner to sell the property quickly. These situations are often attractive to investors like you.
- **Homeowner-centered attorney:** Homeowner-centered attorneys truly represent the homeowner's best interests. They won't file for bankruptcy if the homeowner is unlikely to qualify, and they won't let an investor push the homeowner around. These attorneys know how to play the legal system and can make your life a living hell if you're not pitching what the attorney considers a fair offer.

Getting the homeowners on your side

Bankruptcy protects homeowners from the bill collectors and anyone else who may be perceived as pressuring the homeowners for money or property, including you. If you try to skirt the law and strike a deal with the homeowners, you could find yourself in front of a judge and facing a stiff penalty. Before contacting the homeowners, take the following precautions:

- **Contact your attorney.** Hire an attorney who specializes in bankruptcy and obtain advice on whether you have the legal right to contact the homeowners directly. Also ask for advice and guidelines on how to approach the homeowners and what you can and cannot do as an investor when homeowners have bankruptcy protection.
- **Contact the trustee or homeowner's attorney.** Always keep the trustee or homeowners' attorney in the loop. Present any offer to the trustee or attorney to obtain court approval for the sale.

By establishing a strong relationship with the homeowners, as discussed in Chapter 9, you place yourself in a great position to eventually purchase the property should the homeowners choose to sell it. Don't compromise your good position by trying to work around the bankruptcy attorney or trustee.

Getting the creditors on your side

Homeowners often file for bankruptcy in response to a lender (creditor) initiating the foreclosure process. The homeowners are rarely looking for a way to restructure their payments, and the finance restructuring plans they and their attorneys submit are usually flawed. They're often designed not to enable the homeowner to pay the creditors but to keep the house without paying.

Needless to say, most lenders are not content to patiently watch the bankruptcy proceedings run their course. The lender often challenges the bankruptcy claim and seeks to have the stay lifted, so it can proceed with the foreclosure process. In many cases, they succeed.

When a lender is successful at lifting a stay, the bankruptcy is simply a speed bump in your path to obtaining the property. You may be able to use this speed bump to your advantage. As soon as the homeowners file for bankruptcy and the auctioning of that property is adjourned, many investors lose interest and drop out. If the stay is lifted and the foreclosure proceeds, you may be the only one bidding on the property at auction, and you can buy the property without the worry of a bankruptcy stay. Keep tracking properties, especially when an auction is adjourned, so you're prepared to bid in the event that the property pops back up on the auction block.

Dealing with Bankruptcy Delays on a House You Bought

Although you can work the bankruptcy system to your advantage by purchasing properties through the trustee or the homeowners' attorney, bankruptcy can often delay your ability to take possession of a house you bought at auction. If the bankruptcy court grants a stay, you may be stuck holding a house and paying the bills while the homeowners remain in possession well past the expiration of the redemption period.

In the worst-case scenario, your profit is limited to the interest you charge the homeowners on the purchase price you paid. If the homeowners manage to redeem the property, they must pay you the purchase price plus interest and reimburse you for any property taxes and homeowner's insurance you paid out of pocket.

To sweeten the deal and increase your profit on the property, the best approach is to pitch a deal to the homeowners' attorney or the bankruptcy trustee. Following are a couple suggestions on deals that the homeowners and the court may find appealing:

- **Offer to lease the property to the homeowners.** The homeowners and the courts typically want to avoid a situation in which the homeowners are evicted and have no place to live. By offering to lease the property to the homeowners for a fixed period of time, you demonstrate your sensitivity to their needs and give them a little extra time to find new living arrangements.

- **Structure a buy-back deal.** To avoid a long bankruptcy delay, consider selling the property back to the homeowners at a profit that's perhaps less than what you had hoped for. Why would the homeowners be willing to buy back the house? Because challenging the sale can be costly both in time and money. If the attorney involved can see the benefit of a sure deal that will cost less in the long run, she may be willing to accept it, particularly if accepting the offer ensures she'll get paid. A sure deal looks pretty good next to the alternative — a lengthy and expensive courtroom battle.

When you meet up with a determined and well-qualified bankruptcy attorney, be prepared to negotiate. I've had to deal with attorneys like this, and you can benefit from my experience, as related in the following sidebar, "Playing nice with the sharks."

Playing nice with the sharks

When dealing with a knowledgeable, skilled bankruptcy attorney who's sincerely representing the best interest of her clients, you'd better learn to play nice. I learned my lesson the hard way. Hopefully, you'll learn the easy way by taking heed of my warning and reading my story.

I bought a house at auction and got a pretty good deal on it. About a week prior to the expiration of the redemption period, I received notice that the homeowners had filed for bankruptcy. "No biggie," I thought. I'd seen this before. It simply meant that I would have to wait a little longer to take possession of the property . . . at least that's what I thought.

To my dismay the homeowners had found an attorney who really knew how bankruptcy worked and how to use it to his clients' best advantage. Looking back, I commend the attorney for fighting so strongly and so wisely, but at the time he was a pain in my shorts and my wallet. He managed to drag out the case for weeks on end. While his clients remained firmly planted in the house, I was footing the bill.

Just when I thought we would be wrapping the whole thing up, I was told that the homeowners would be seeking a jury trial. Now I'm no attorney, and I don't know what entitles you to a jury trial, but I knew that a jury would quickly see me as the big bad investor preying on the helpless insolvent homeowners, even though the homeowners got themselves into this mess and I did everything by the book. To add insult to injury, the attorney whispered to me at the preliminary hearing that the judge scheduled to hear the case would be heading to China for a three-week vacation.

I almost popped a gasket. I did everything right, I had to defend myself in court, and now I was going to have to wait for Marco Polo to return from China to hear my case! That night, I stewed the defensiveness right out of me and decided to stop fighting the system. The next time the attorney contacted me, I asked him, "Do your clients want to just buy back the house so we can put this behind us?" The attorney responded, "I thought you'd never ask! We can probably wrap this all up before her honor goes on holiday."

The attorney was able to structure a deal for his clients that allowed them to keep their house, and I was able to make a fair profit on the buy

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back price. We obtained court approval, and the whole fiasco disappeared as quickly as it had first surfaced. The attorney and I have developed a relationship since then, and he explains to me that he could easily have kept that property tied up in the courts for two years, and maybe I wouldn't have even gotten the house.

The moral of the story is that when meet up with a stubborn attorney who knows his stuff, don't dig in your heels and flex your muscles. You may need to take a different approach. Keep your eyes on the prize — in this case, the profit — and don't let anger or self-righteousness drive you into taking a no-win stance. Remain flexible and look for win-win solutions.

REMEMBER

As a general rule, I don't like to be involved in bankruptcy buys, not because there isn't money to be made, but because I find that other investment opportunities are much more attractive and give me fewer headaches. Many real estate investors like me also shy away from bankruptcy properties, however, and that's exactly the reason why some investors are so successful in this area — they have less competition. If you do decide to work in the bankruptcy arena, develop a strong knowledge of how bankruptcy works in your area and don't go it along — hire an experienced bankruptcy attorney to serve as your Sherpa.

Chapter 15

Sampling Some Other Foreclosure Strategies

In This Chapter

- Selling short to boost your profit
- Buying and selling second mortgages and other junior liens

Throughout most of this book, I encourage you to purchase properties directly from homeowners prior to auction or bid on properties at auction — to purchase senior liens. You can also make money in foreclosures and improve your position as an investor by

- Negotiating short sales — convincing lenders to accept a payoff of less than the full amount owed.
- Purchasing junior liens — second mortgages and other claims against the property.
- Acquiring tax deeds or liens — paying back taxes to obtain a tax deed or lien against the property.

These strategies may even enable you to earn a profit without ever taking possession of the property and having to deal with the hassles of owning, selling, or leasing the property. They can also strengthen your position in acquiring the senior lien and eventually taking possession of the property.

Buying junior liens without buying the senior lien is risky. If another investor buys the senior lien and foreclosure wipes out the junior liens, you can end up owning a worthless piece of paper. Don't buy junior liens until you've read through the following section and have some experience buying senior liens.

Negotiating Short Sales

Your parents probably told you never to "sell yourself short," meaning that you shouldn't accept less than what you're worth. When you're investing in foreclosures, however, you want the lien holders to sell themselves short by agreeing to negotiate *short sales* — accepting less than they're owed.

Lien holders who stand to lose something if a property goes into foreclosure are often willing to accept less money than they're owed. After all, less is better than nothing or continuing to throw good money after bad.

In the following sections, I reveal the hierarchy of lien holders, so you know which liens hold the most weight in foreclosure. I show you how to recognize situations that are ideal short sales opportunities, and then I guide you through the process of collaborating with the homeowners and lien holders to structure a deal that meets the needs of everyone involved, including you.

Don't start negotiating short sales until you've done your research on the property, as discussed in Chapter 8, and carefully research the title. If you overlook a single lien on a property, it can come back to bite you . . . or at least bite a big chunk out of your profit.

Knowing the lien holder pecking order

Lien holders all lay claim to a property, but all liens are not created equal. By assessing the strength of each lien holder's position in line for receiving payment, you place yourself in a superior position to negotiate. Think of lien holder positions as the value of each card in a deck of playing cards:

- **Ace:** The property tax collector generally holds the Ace, because foreclosure can wipe out all other liens except the property tax lien. If you can purchase the tax lien, you almost always hold controlling interest in the property. The tax lien holder, however, must adhere to some strict regulations regarding the notification of other lien holders.
- **King:** The lender with the first mortgage on the house holds the King. The first-mortgage holder can always pay any back taxes that are due, purchase the property at auction if nobody bids on it, wait for the redemption period to expire (and wipe out the junior liens), and then sell the property.
- **Ten:** The lender who owns the second mortgage (if a second mortgage is in place) holds a Ten, but if the lender stands to lose a great deal of money, the lender may be motivated to buy the first lien and pay any back taxes to strengthen its position. The holder of a second mortgage, however, is in a very weak position if the house isn't worth the combined value of the first and second mortgages but is worth the value of the first mortgage. In such a case, the lender who owns the first mortgage has little motivation to negotiate with the owner of the second mortgage.

- **Three:** Construction (mechanic's) lien holders typically are the big losers in foreclosure. Because foreclosure wipes out their position, they become more and more motivated to negotiate a short sale as the foreclosure sale or the end of the redemption period looms. If the homeowners agreed to put up the construction asset as collateral for the loan, however, the lien holder may qualify for a step up in position. For example, if the homeowners took out a loan to build a new room on the house, that new room may be what's called a PMSI (Purchase Money Security Interest) that the construction lien holder can lay claim to. This is a very complicated situation, so if you encounter such a situation, consult your attorney.
- **Two:** Legally speaking the IRS may have a stronger position than the second mortgage or construction lien holders, but they rarely step in and buy the property, so they hold the weakest card in the deck. The IRS must be notified and offered the chance to purchase the property, but that's not likely to stop an auction from going forward. If you are not confident that the IRS received a proper notice prior to the auction, you may want to hold off on buying the property.

The lien hierarchy is determined primarily by the dates on which loans are recorded against a property. The property tax lien is the strongest position, typically followed by a first mortgage, because that's the loan the homeowners took out to buy the property, and then followed by other loans in order of the date on which loan was recorded. In other words, if the homeowners took out a first mortgage to buy the house, then financed new windows, and then took out a second mortgage, you would probably be looking at the following hierarchy (listed from strongest to weakest):

- Property tax lien (strongest).
- First mortgage.
- Construction loan (new windows).
- Second mortgage (weakest).

Of course, you can always have exceptions. The window company, for example, may have and often does subordinate its position to the second mortgage holder, or the holder of the second mortgage may pay the window company to "step up" into its position. Check the dates of recording on the mortgages and look for any wording that specifically states whether one mortgage is subordinate to another.

WARNING!

Don't confuse the date the mortgage was taken out with the date it was recorded. If a mortgage is taken out in June 2005 and isn't recorded until June 2006, and in between those two dates another mortgage is taken out and recorded, the mortgage taken out in June 2005 loses its priority position. Other conditions and exceptions may come into play, so when you're just starting out, consult a real estate attorney who has plenty of experience deciphering titles and mortgages.

The lien holder pecking order is important because it determines the winners and losers after the auction — who gets paid and who doesn't. Say a $200,000 property has a $6,000 tax lien against it, a $140,000 first mortgage, a $20,000 second mortgage, and a construction lien of $10,000. At the tax sale, an investor may bid $160,000 for the $6,000 tax lien. The tax collector gets the first $6,000, the first mortgage lender gets $140,000, the second mortgage lender gets $14,000, and the holder of the construction lien walks away with nothing.

Of course, this example is a little odd, because the first mortgage holder would probably pay the $6,000 in back taxes to protect their position rather than let an investor buy the tax lien. I provide the example only to illustrate who ends up with money and who doesn't based on the strength of their claim to the property.

REMEMBER

Tax sale rules vary from state to state. In some states, the tax sale wipes out all other liens, so if you buy the property at a tax sale, anything you pay in excess of the taxes owed on the property goes to the state, and the other lien holders receive nothing. Of course, prior to the tax sale, the other lien holders must be notified that their claims to the property will be wiped out by the tax sale, so any lien holder with a major interest in the property is likely to pony up the unpaid taxes. Consult your real estate attorney to find out more about how tax sales are handled in your area.

Wheeling and dealing with lien holders

The lien holder pecking order is also very important to know when you're dealing with multiple lien holders who are all trying to protect their position. Keep in mind that any lien holder who's lower on the pecking order has the right to buy out the positions of the other lien holders simply by paying off the balance of the money owed them and any interest and associated costs.

Say three lien holders (A, B, and C) have a stake in the property, with A holding the highest position and C holding the lowest. Depending on how much equity is built up in the property, any of several scenarios can develop, including the following:

- You buy A's position (either at auction or directly from A) and wait for redemption period to expire. B and C take no action, and their positions are wiped out.
- You buy A's position. B buys you out to protect its position and waits for redemption period to expire to wipe out C's position. You have to sell, but you don't have to discount, so you should at least get your money back.
- You buy A's position. C buys out both you and B to protect its position.

- Another investor buys A's position. You buy B's position, giving you the right to buy A's position from the other investor, which you do, forcing C to either buy you out or lose out entirely.
- You buy A's position and then buy B's and C's position (typically by paying them less than the total of what they're owed via a short-sale agreement). Why buy out B and C? If the property has a lot of equity in it, buying out B and C prevents them from buying your position and prevents other investors from buying B's or C's position and then attempting to buy you out.
- You buy A's position, and then, during the redemption period, the homeowner redeems the property (buys you out).

As you can see, the wheeling and dealing can get pretty complicated. Later in this chapter, in the section "Negotiating with the lien holders," I show you how a typical negotiation is likely to play out.

Recognizing a short sale opportunity

Some scenarios are more conducive to short sales than others. If the property has little equity in it and is unlikely to draw bids at auction, the senior lien holder is looking at getting stuck with the hassle and cost of preparing the property for market and selling it. They may prefer to accept less than the full amount owed just to cut their losses.

If the senior lien holder has no reason to bargain, you may be able to strengthen your negotiating position by working out short-sale agreements with junior lien holders. If a bank holds the senior lien on a very valuable piece of property, for instance, the bank probably won't accept less than the full amount owed on the property. By convincing junior lien holders to accept less than the full amount owed on their loans, you may place yourself in a position in which you can afford to buy out the senior lien holder's position. Following are descriptions of situations that are excellent opportunities for negotiating short sales with junior lien holders:

- **The property has two or more liens on it, and the senior lien holder is foreclosing.** This starts the clock ticking for the junior lien holders. Unless they purchase the senior lien holder's position, they stand to lose everything. An offer from an investor like you to a junior lien holder, even if that offer is for 30 or 40 cents on a dollar, is better than nothing.
- **Unpaid taxes have driven the homeowners into foreclosure.** Again, the junior lien holders are in the unsavory position of having their interests wiped off the books.

- **The senior lien is larger than any of the junior liens.** If a junior lien holder has more to lose than the senior lien holder, the junior lien holder is likely to buy the senior lien holder's position rather than negotiate with you for pennies on a dollar. When the senior lien is much larger, however, the junior lien holder rarely ties up more of its money by buying the senior lien position and is more likely to negotiate with you.
- **Multiple junior lien holders lay claim to the property but the senior lien is not worth more than 75 percent of the property's market value.** All the liens can total more than the house is worth, but if the senior lien position gives you at least a 25 percent profit margin to negotiate, the lien holders should be willing to work with you.

Teaming up with the homeowners

You can't negotiate short sales without the homeowners' cooperation. They must sign a release, provided in Chapter 9, giving you permission to discuss their finances with the lien holders and negotiate short sales on their behalf. Let the homeowners know that by empowering you to negotiate the short sales, they retain more control of the situation, may be able to avoid foreclosure, and, if they eventually decide to sell the property to you, stand to earn more money from the transaction.

REMEMBER

You may be able to purchase a lien holder's position directly from the lien holder without the consent or cooperation of the homeowners, but if you're working on behalf of the homeowners, most lien holders cannot and will not discuss the situation with you until they have a signed authorization from the homeowners. If you happen upon a lender willing to sell you seconds (second lien holder positions), keep the information under lock and key — buying seconds can be an effective strategy for gaining control of a property. See "Buying and Selling Junior Liens," later in this chapter.

Before you start calling lien holders, consider how you're going to profit from the short sales. You can profit in any of the following three ways:

- **Buy the house.** Present the homeowners with your offer to purchase the property conditional upon your ability to successfully negotiate the short sales. See Chapter 10 for details on presenting your purchase agreement.
- **Charge the homeowners for your services.** Contract with the homeowners to negotiate the short sales for a fee. Consult your real estate attorney to draw up a suitable contract.
- **Foreclose on the house yourself.** If the homeowners aren't willing to work with you, you can still negotiate with the lenders and perhaps purchase the first mortgage position, giving you the right to foreclose and ultimately take possession of the property. You can even buy a junior lien and foreclose on the house, but be careful and check out "Buying and Selling Junior Liens," later in this chapter, before attempting this strategy.

WARNING!

Without a purchase agreement in place, you may negotiate the short sales, getting the homeowners out of foreclosure, and then have the homeowners say "Thanks," and cut you out of the deal. Unless you own the property tax lien or the first mortgage lien, always have a signed purchase agreement with the homeowner or a signed contract stating how the homeowners will pay you if you are successful in negotiating short sales that save them from foreclosure.

Gathering payoff amounts

The first step in negotiating short sales consists of gathering some basic information — the amount required to pay off each loan in full by a specific date. Call each lien holder and ask them to explain the procedure for requesting payoff amounts.

In most cases, the lien holder requires that you fax or mail a letter to the lien holder. In your letter, provide the following:

- Borrowers' names
- Account number
- Property address
- Date of payoff
- Your contact information
- The signed release from the homeowners giving the lender permission to share the information with you
- A request that the payoff letter be faxed or mailed to you

WARNING!

Specify a payoff date that's at least one month away or a day or two before the homeowners are due to lose their home in foreclosure, so you have time to negotiate with other lien holders. All of your negotiations should be wrapped up prior to the payoff date; otherwise, a lien holder may retract its offer. Give yourself plenty of time to negotiate.

Crunching the numbers

When you receive the payoff letters from the lien holders, you now know exactly how much the homeowners will owe on the payoff date. With this information in hand, you're now ready to calculate the total amount required to pay off all balances in full. Use the form in Figure 15-1 to perform your calculations. Figure 15-2 shows a completed form.

Property Owner Names: ____________________

Property Location: ____________________

Foreclosure Sale/Redemption Date: ____________________

Payoff Date: ____________________

Property Value: ____________________

Lien Holder Name	Payoff Amount
Total	

Figure 15-1: Calculate the total payoff amount.

Property Owner Names: Liz and Peter Henderson

Property Location: 1313 Mockingbird Lane

Foreclosure Sale/Redemption Date: May 31

Payoff Date: May 20

Property Value: $144,000

Lien Holder Name	Payoff Amount
City Mortgage (first mortgage)	$84,349.42
Capital Source (second mortgage)	$39,208.16
Jackson Heating & Cooling	$10,680.00
Internal Revenue Service	$16,803.43
Total	**$151,041.01**

Figure 15-2: Calculate the total payoff amount.

If you don't know how much you're prepared to pay for the property, refer to Chapter 10 to project your profit and determine a maximum amount you're willing to pay. You can then work back to adjust the short-sale payoff amounts.

TIP

As a general rule, the lower the lien holder's position in the pecking order, the bigger the discount he's likely to accept.

Say you perform your calculations using the Deal Analysis Worksheet in Chapter 10 and decide that your top offer for the property would be $111,600.

Using the information shown in Figure 15-2, you can now work backward to identify opportunities for short sales:

- The balance on the first mortgage from City Mortgage is $84,349.42. Because the estimated property value is $144,000, City Mortgage is highly unlikely to agree to a short sale. It would be better off owning the property. You're going to have to pay the full $84,349.42. That leaves you about $27,251 for paying off the other lien holders without exceeding your top offer of $111,600.
- Capital Source holds the second mortgage of $39,208.16. This is a perfect opportunity for a short sale. Capital Source stands to lose the entire amount of the foreclosure proceeds to conclusion and the homeowners fail to redeem the property. They may be willing to accept $24,000 to assign the lien to you, in which case the homeowners owe you the $39,208.16. This places you in a prime position to buy the first mortgage at auction. See the following section for details.
- Jackson Heating & Cooling holds a construction lien of $10,680.00. It's in a very weak position and is unlikely to buy the first mortgage of $84,349.42 to protect its position. It would be very likely to sell you its position for $2,000–$3,000.
- The IRS is also unlikely to invest $84,349.42 to protect its $16,803.43 position. If you can convince the IRS to release its claim, you won't have to pay them a cent.

Assuming your negotiations unfold according to plan, you pay City Mortgage $84,349.42, Capital Source $24,000, and Jackson Heating & Cooling a cool $3,000 (at the most), for a grand total of $111,349.42, slightly below your target of $111,600.

Negotiating with the lien holders

When you know where all the lien holders stand, you can begin calling them and negotiating your short sales. You can't negotiate the property tax lien, but you can negotiate short sales on the other liens. The following sections provide some guidance on how to proceed, but every situation is different, so use your noodle and plan the strategy that you think is likely to be most effective.

TIP

If you have a purchase agreement signed by the homeowners stipulating that the sale of the property hinges on your ability to successfully negotiate short sales, present copies to the lien holders. Explain that you're structuring a deal to minimize the lien holders' losses and that all of the lien holders must agree to the deal for it to succeed . . . and for them to receive payment.

If the property has a property tax lien against it, use that to your negotiating advantage. Tell the lenders that if they don't work with you, they can expect to incur another $5,000 expense (or however much the tax lien is). This lets the lender know that it can automatically offer you a $5,000 discount without losing anything. To make it worth your while, request a discount in excess of what's owed in property taxes. If the lender discounts from $25,000 down to $20,000, and you have to pay $5,000 in taxes, you're not really getting anything. If it discounts down to $17,000 or $18,000, you immediately increase your profit margin. Crunch the numbers, stick to your guns, and remember that the closer you get to the date on which the junior lien holder is scheduled to lose everything, the more negotiating power you have. Just be sure you're able to act quickly and buy the first mortgage to protect your position, or you'll lose everything.

When buying liens, request an assignment of interest or assignment of lien or mortgage from the lien holder and have your attorney look it over and approve it before proceeding and before handing over the check. After obtaining the assignment, run it down to the register of deeds or county clerk's office to have it recorded.

Negotiating a release with the IRS first

The IRS is often willing to release its lien on the property, simply because it's not all that interested in buying the first lien to protect its position. In addition, the IRS may be able to pursue the homeowners for unpaid taxes even if its lien is wiped out by the foreclosure.

Call your local IRS field office and request the name and contact information for the person in charge of real estate liens. Call the person in charge and ask whether the IRS would release its lien if the property changes hands. Unless the amount owed to the IRS is huge and the property is worth enough to justify the IRS paying off the first lien, it's likely to agree to releasing its lien. Just make sure you get the release in writing.

REMEMBER

The IRS is likely to release its lien and its usually takes the longest to get back with you, so contact the IRS first. While you're waiting to hear from the IRS, continue negotiating with the other lien holders.

Dealing with first mortgage lenders

Because the first mortgage holder is near the top of the lien holder pecking order (just below the property tax lien), it acts as puppet master, pulling the strings that control the entire outcome. In some cases, however, even the first lien holder's position can be weakened, such as in the following scenarios:

- **The property is not worth significantly more than the first mortgage payoff.** If the remaining balance is $85,000, and the home is worth only $15,000 more than that ($100,000), the bank is unlikely to profit much by taking possession of the property and selling it. The repairs and holding costs alone are likely to gobble up that $15,000, and the bank won't want the hassle.

- **The unpaid property taxes are high.** Remember, the property tax collector gets paid first. If the homeowners owe $30,000 in property taxes on a house that's worth $150,000, and the first mortgage balance is $105,000, the bank would have to pay $135,000 to acquire the property and would stand to gain a maximum of $15,000 minus the costs to repair and sell the property.

If you crunch the numbers and the result shows that first lien holder has something to lose or at least nothing to gain from the foreclosure, contact them, lay out the numbers, and consider offering to buy their position for less than the full payoff amount. Once you take possession of the first lien and pay the back taxes, you have control of the property. If the homeowners refuse to sell the property to you, you can foreclose on them. Even if they redeem the property, you earn a profit, because you purchased the note for less than the full payoff amount.

Don't overlook the tax lien. If you purchase the first mortgage and forget to pay any property taxes that are due, another investor can buy the tax lien and cut you out of the deal. Make sure nobody has purchased the tax lien and then calculate the back taxes into the equation. You want to make sure that if the homeowners do redeem the property, you're still in a position to profit from the deal.

Contacting construction lien holders

Construction lien holders, like Jackson Heating & Cooling (see Figure 15-2) are often difficult to deal with. They've been stiffed by the homeowners, and their emotions run high. They may not understand the foreclosure process and are often reluctant to deal with an investor who's offering pennies on a dollar.

The most effective way to negotiate a short sale with a lien holder who's in a weak position is to let the facts speak for themselves. With Jackson Heating & Cooling, for instance, you could say something like, "I'm negotiating with the senior lien holder. If they agree to sell to me I won't need to buy your position at all. If you decide to sell to me before I work out a deal with the senior lien holder, then I'll honor that deal. You could pay off the first and second mortgages to the tune of $123,557.58, foreclose on the property, and hope to recover your loss by selling it, but that's a costly proposition both in time and money. You could do nothing and I could almost guarantee that you'll lose your entire $10,680 at the foreclosure sale. Or, you can accept my offer of $3,000. I'm not trying to play hardball, but I wanted to give you the option to make an informed decision. I understand the position you're in with not being paid for the quality work you've done." Any reasonable person would take the $3,000.

Contacting other major lenders

Lenders who hold second or third lien positions on the house (second or third mortgages) are next in line to get paid. The first challenge you face in dealing with these lien holders is tracking down the person in charge of making the decisions. At a larger bank, ask to speak with the manager of the foreclosures or loss mitigation department. At smaller banks, request to speak with the person in charge of buying and selling mortgages.

Dealing with major lenders is often easier than dealing with small businesses, such as those that may be holding construction liens, because major lenders know how the game is played and are often less emotionally involved. They take a rational look at the numbers, know what they have to lose in foreclosure, and understand what they have to gain by working with you. Major lenders are often willing to sell you the mortgage note (promise to pay) at a discount to cut their losses and pass the problem along to you.

Take a look at the numbers in Figure 15-2. Capital Source holds the second mortgage of $39,208.16, which it stands to lose in foreclosure. It's going to be highly motivated to agree to a short sale, so it walks away with something.

Say the IRS releases its lien of $16,803.43 and Jackson Heating & Cooling sells its position to you for $3,000. You now have $24,250.58 remaining to buy Capital Source's position and hit your target of paying $111,600 for the house. Sure, your offer is $15,000 short of the second mortgage payoff amount, but Capital Source gets a sure thing — over $24,000 — and it doesn't have to worry about losing everything in foreclosure.

Capital Source can respond to your generous offer in any of several ways:

- **Reject it outright.** Not likely, because you showed them the numbers, and this is the most they can hope to get out of the deal.
- **Release the lien.** They agree to accept your offer as full payment. You pay off the mortgage balance to City Mortgage. You pay Jackson Heating & Cooling its $3,000, and the IRS releases its lien. You close on the house and are now the proud owner of an investment property.
- **Assign the mortgage note to you.** Assigning the mortgage note consists of passing the ownership of the debt to you, which places you in an excellent position for buying the first mortgage at auction. You don't even have to pay Jackson Heating & Cooling the $3,000, because you now hold a higher lien position. That extra money can come in handy when auction day rolls around.

The concept of assigning a mortgage note is a little complicated, so here's an example of how it could play out in our example:

- You buy the mortgage assignment for $24,000.
- When the first mortgage goes up for auction, bidding is likely to start at about $84,000 — the full payoff amount to City Mortgage.
- You bid $123,000, because you own the $39,208.16 debt assigned to you by Capital Source. ($84,000 first mortgage plus $39,000 debt assignment equals $123,000.) Why bid so high? See the next bullet item.
- Nobody is likely to outbid you, because the profit margin just isn't there, but if someone does outbid you, you still profit. Here's how it works: By bidding $123,000, you guarantee yourself an overbid of $39,000. If nobody outbids you, you own the house and can then apply for the $39,000 in overbid money, which you are eligible for as the second lien holder. You end up paying $108,000 for the house ($84,000 plus the $24,000 you paid to Capital Source). If someone does outbid you, you still collect the $39,000 overbid. Subtract the $24,000 you paid for the assignment of debt, and you earn a $15,000 profit free and clear.

How do you earn a $15,000 profit? Doesn't that overbid money go to the homeowner? Overbids are paid out first to the lien holders. The homeowner is the last in line to receive anything, assuming money is left over. When you negotiated with Capital Source to accept $24,000 in payment to assign its mortgage note of $39,000 to you, you set yourself up to earn $15,000 in the event that anyone bid more than $123,000 on the first mortgage.

So, what happens to Jackson Heating & Cooling's lien? It's wiped off the books, because that lien is paid only if the overbid exceeds the amounts needed to pay off the first and second lien holders.

Buying and Selling Junior Liens

One of the most common and costly mistakes that novice investors make at auctions is to buy a junior lien thinking they're buying a property. Because junior liens are often wiped out by foreclosure, these uninformed investors often purchase a worthless piece of paper. If you know what you're doing, however, you can purchase seconds (junior liens) to gain control of a property or even earn a profit without taking possession of the property.

Don't buy a junior lien without buying the senior lien and paying any overdue property taxes, as well. If someone else buys a lien that's higher up in the pecking order, you stand to lose your entire investment if you don't buy them out prior to the end of the redemption period. If your area has no redemption period or the redemption period expires before you redeem the senior lien holder, you lose all of your money. I strongly urge novice investors not to buy junior liens until they've gained some experience buying senior liens.

Buying junior liens to foreclose for a quick payday

Some investors like to roll the dice and gamble on buying *seconds* (junior liens) at a discount in the hopes that the homeowners will redeem the liens to avoid losing their homes. This strategy offers several benefits:

- Nobody else wants them.
- They're affordable — typically \$2,000–\$15,000 instead of \$100,000+.
- Most of the time, the homeowners redeem the junior lien, which means you earn the difference between what you paid for the lien and the foreclosed upon amount — usually the face value of the lien plus interest. Because the interest rate on junior liens is typically higher than the interest rate on first mortgages, even if you earn only the interest, you're usually getting a better return on your money than if you had invested it elsewhere.
- If the homeowners don't redeem, the equity in the property may be sufficient to buy the first mortgage and recoup your investment plus a profit. This is definitely something you want to know before you buy.
- You gain a controlling position in the property.

Buying junior liens, however, has several drawbacks, as well, including these:

- If most homeowners redeem, you rarely gain possession of the property.
- If someone else buys a senior lien, you stand to lose your entire investment.

To take advantage of this strategy, search for junior liens that are in default already or that will soon be in default. If the homeowners continue to make payments on the loan, you can't foreclose. As you can see, this is a bit of a gamble.

Never buy a second if you're not prepared to pay off the first mortgage or walk away from the deal chalking up your investment as a loss.

Personally, I'm not fond of this strategy. For me, having controlling interest in the property is my prime motivation for buying a second. By purchasing the second, I force the senior lien holder to deal with me, and I can always pay them off and take them out, giving me the pole position. You have to know what you're doing, though, or you can really get burned if someone swoops in and buys that first position.

Witnessing a train wreck

At one auction I attended, I noticed a new buyer who seemed very interested in a property that I knew was a second mortgage. Out of my love for my fellow man I asked him if he knew what he was buying. From his response I could tell that he was a newbie. I told him that he was going to bid on a second and asked if he knew what that meant. I wasn't able to convince him that he was making a mistake, but it was his money. I made one last attempt, I told him, "Tell you what, you give me half of what you're going to bid today, I'll punch you as hard as I can in the gut, and in six months you'll look back and thank me. Or you can buy that second, and in six months and tens-of-thousands of dollars poorer, you can wish you would have listened to me." It didn't work. I think he thought I was competing for the property and trying to convince him to bow out.

I ran into the same guy about a year and a half later and asked him how his investment turned out. "Not well," he said.

"How much?" I asked.

"Around $18,000 and eight months of headaches," he replied, "I should have taken that punch in the gut. In fact, I'd take a kick a little lower if I could get that money back." I just laughed, but this is no laughing matter. Know what you're buying and avoid buying yourself in over your head.

Buying seconds to protect the first mortgage

If you buy a first mortgage and the property has enough equity in it even after accounting for the second mortgage, another investor can swoop in, buy the second, pay you off, and walk away with the property. You don't lose the money you paid for the first mortgage, but you do lose the property and the opportunity to earn a bigger profit. When you buy a first mortgage on a property that has sufficient equity to tempt another investor to buy the second, you can employ any of the following strategies to protect your investment:

- **Pay off the second mortgage.** If the second mortgage is low enough, you may want to simply pay it off. I'm not saying you should always pay off the second mortgage, but if you crunch the numbers and can still earn a tidy profit, this is an option.
- **Buy the second mortgage at a discount.** You may be able to buy the second mortgage at a discount from the lien holder or, if the lien holder forecloses on the property, you may be able to buy it at auction to protect your position. If the lien holder is unwilling to sell short, let him know that you own the senior position and that if the homeowners don't redeem, he stands to lose everything.

- **Convince the owner of the second mortgage not to sell to another investor.** Contact the second lien holder and let her know that you purchased the first and that if nobody redeems your mortgage and the second lien holder agrees not to sell or assign its position, you will pay her some fixed amount (as determined in your budget). If she agrees, have your attorney draw up an agreement. This prevents another investor from buying the second and then redeeming the first mortgage. This strategy offers two benefits: You don't have to come up with the money upfront to buy the second mortgage, and the second lien holder doesn't have to give up her position — if the homeowners redeem your first, the second lien holder retains its position and can now foreclose for full value rather than selling short to you.
- **Overbid enough at the sale to satisfy the second mortgage.** You can essentially pay off the second mortgage by bidding enough to satisfy that debt or provide enough money to the second lien holder, so redeeming you or selling their position to another investor would not be worth the time and hassle.

Selling a junior lien for a profit

If the thought of taking possession of the property doesn't appeal to you, you can deal exclusively in paper by buying and selling junior liens. For example, you may be able to negotiate a short sale with a junior lien holder, convincing the lender to accept something like a $10,000 payment on a $25,000 lien. You can then turn around and sell the junior lien to another investor for $15,000, earning a $5,000 profit without ever touching the property.

WARNING!

Before venturing into the uncharted waters of buying and selling mortgages, consult with your real estate attorney to make sure you're set up to do it legally. Certain areas may have restrictions on the number of mortgages a private individual can hold at one time.

Profiting from Property Tax Sales

When homeowners fail to pay property taxes, the taxing authority places a powerful lien against the property that almost always supersedes all other liens. While other liens can get wiped out by foreclosure, the property tax lien cannot.

Unfortunately for you, as an investor, a tax lien may never end up on the auction block. Another lien holder is highly unlikely to see its position wiped out because of a few measly dollars in unpaid taxes. If the lender with the first mortgage has a major stake in the property, the lender is usually going to pay the back taxes and then file an affidavit to add the taxes to the first mortgage payoff amount — the amount the homeowners would have to pay to redeem the property.

To profit from tax sales, research the property carefully prior to the auction, as discussed in Chapter 8. Then, do some additional homework, as explained in the following sections to track down tax sales, find out the way tax sales are handled in your state or county, and locate tax sale opportunities.

Although purchasing tax liens is a relatively low-risk approach to acquiring foreclosure properties and profiting from foreclosures in other ways, you can still get burned when purchasing tax liens, especially if you don't know the rules, regulations, and deadlines that apply to tax sales in your area. The following section shows you how to find out much of the information you need, but you should also consult an attorney and have a clear understanding of the process before buying tax liens.

Tracking down property tax sales

Delinquent property taxes are almost always processed at the county level, so your county offices are the most logical places to find information about tax sales. If your county has a website, it should supply most of the information you need, so the clerks don't have to spend most of their days answering questions.

If no Web site is available, you can try contacting the tax assessor or commissioner, the delinquent-tax department, the treasurer, or the sheriff, but these offices generally shy away from providing details, because they don't want to be accused of "giving legal advice." Your best bet is usually to consult your real estate attorney.

When you finally locate a quality information resource, gather information to answer the following questions:

- Where and when are the tax sales?
- Do you sell tax deeds or tax lien certificates? (See the following section for more about the difference between tax deeds and certificates.)
- Does the tax lien hold priority over all other liens? If not, which liens can supersede it?
- If I buy a tax lien, do I need to do anything to protect my position on the title? Do I have to record my interest? Do I have to buy future tax lien certificates as they go to sale?

- How long is the redemption period on tax sales?
- Can I do anything to shorten the redemption period, such as have the homeowners sign a non-redemption certificate?
- What do I need to do to take possession of the property after the redemption period expires?
- If I have to evict the homeowners, how much does eviction cost?
- What percentage of homeowners redeem?
- If the homeowners redeem, do they have to pay interest and penalties? If they do, what's the percentage and fees and how much of that do I receive upon redemption?
- How can I obtain a list of properties scheduled for the tax sale?
- What are the purchasing terms on tax liens at time of sale?
- Do I have to register as a bidder in order to bid?
- Does the county offer financing to purchase tax liens?
- How does the bidding work? Is it a sealed bid or open auction?
- Are any other costs added to the back taxes? If so, are those costs added to the total before bidding begins or after it's completed?
- What happens to properties that don't sell at auction? Can I buy them directly from the county? If so, how do I go about placing an offer? Can I get a list of the properties?

TIP

Pick your real estate attorney's brain for additional information and advice concerning tax sales in your area. Because your attorney's job is to protect your interests, your attorney can highlight the pitfalls and perhaps offer tips to succeed that are specific to the tax sales in your area.

Finding golden tax sale opportunities

When most people buy a house, the lender requires the creation of an escrow account out of which property taxes and insurance are to be paid, because the lender knows that homeowners often forget to set aside enough money to pay their property taxes or they simply forget to send in their payments.

When homeowners fall behind on their property taxes, unpaid taxes along with the penalties and interest quickly add up, particularly if the homeowners are behind on their mortgage and other bills. In some cases, the homeowners may not even be receiving the notices that their property taxes are due. Perhaps the owner died and the family is unaware that taxes are due, or the homeowners live out of state. In these situations, the tax lien may be the only lien on the property. As an investor, this can be a perfect opportunity for acquiring the tax lien and buying a property for much less than market value.

TIP

Pay particular attention to tax liens on properties that have no other liens against them, abandoned properties, properties with out-of-state owners, and properties that the owners use as their vacation home. In the case of a property used as a vacation home, the homeowners facing foreclosure may be using all of their resources to save their primary residence, so they drop the ball on the vacation home.

Buying tax deeds or certificates?

One of the most important differences in how tax sales are handled from state to state is whether the state sells *tax deeds* or *tax certificates*:

- A *tax deed* is a document conveying ownership of the property to the high bidder. Prior to the tax deed sale, the county informs the homeowners and all lien holders that the property is going to be sold if nobody pays the past taxes. In most cases, a lien holder who has a large claim on the property pays the back taxes. If nobody pony's up the money to pay the taxes, the county auctions off the tax deed.
- A *tax certificate* or *tax lien* is simply a document giving the purchaser the right to collect the unpaid taxes. When you buy a tax certificate, you're essentially paying the taxing authority to take over its interest in the property. This gives you first lien position on the title. You can then foreclose on the property or place yourself in a better position with the homeowner and other interested parties to acquire the property.

Getting redeemed out of your position

When you buy a tax deed or lien, you may begin to feel as though you won the lottery. You now control the property and can cut all junior lien holders out of the deal. You're on easy street, right? Not quite.

In a large percentage of cases, the homeowners redeem the tax deed. This isn't all that bad. Worst case scenario, you get your money back. In some areas, the homeowners may also have to pay penalties and interest, some of which you may be entitled to. In other words, you stand to profit even if you lose your interest in the property.

To encourage investors to purchase them, tax liens typically carry a very high interest rate or are auctioned off for only a fraction of what's owed in back taxes, so investors can earn a worthwhile profit. If the homeowners or other lien holders don't redeem the tax lien, it may convert to a tax deed, allowing the holder to take action to gain possession of the property. Tax deeds may have no redemption period or a period that's shorter than that of tax liens.

Profiting from the tax lien or deed

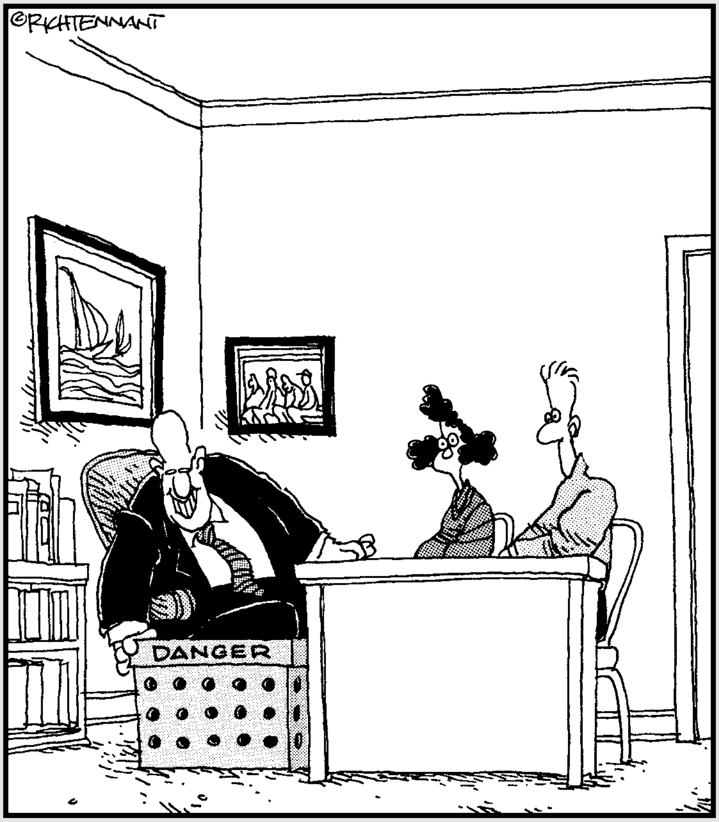
Once you own a tax deed or lien, how do you profit from it? Following are various strategies for profiting from a tax lien or deed:

- Take possession of the property after the redemption period expires, and repair, renovate, and sell the property.
- Sell the tax lien or deed to another investor or one of the other lien holders for a profit.
- Sell the tax lien or deed to the homeowners for a profit.

Part V

Cashing Out Your Profit . . . after the Sale

The 5th Wave By Rich Tennant



"Let's see if we can determine your capacity for assuming risk. Now, how familiar are you with snake handling?"

In this part . . .

You may make your money when you buy a foreclosure property, but you don't realize the return on your investment until you sell the property, lease it, or refinance to pull some or all of the equity out of the property.

The chapters in this part focus on the property after the purchase. Here you pick up some strategies for easing the previous homeowners out the door or evicting them when they refuse to leave. I show you how to maximize your profit by repairing, rehabbing, and then either leasing the property or selling it. Finally, I reveal various ways to cash out on a foreclosure transaction without leasing or selling right away.

Chapter 16

Assisting the Previous Homeowners Out the Door

In This Chapter

- Attending to details after the purchase
- Securing your property through the redemption period
- Laying the groundwork for repairs and renovations
- Ushering the previous homeowners out the door

After working so hard to find a foreclosure property and negotiate with homeowners and lenders or submit the winning auction bid, you may think that you're home free. You are now the proud owner of a valuable investment property that you can repair, renovate, and either rent out or sell for a profit.

Whoa! Slow down. After purchasing a property, you now have to tie up any loose ends to secure your purchase:

- If the homeowners accepted the price and terms of your purchase agreement, you have to close on the home. See Chapter 19 for additional details on the closing process.
- If you purchased the property at auction, you must satisfy the terms of the purchase, pay any back taxes, and file some additional paperwork. See "Tying up the loose ends after the auction," later in this chapter.
- If your state has a redemption period, you must fulfill your responsibilities until the redemption period expires, as discussed later in this chapter in the section "Protecting Your Investment through Redemption."
- If the property is vacant, you have to make sure it's safe, secure, and insured. See "Securing the property," later in this chapter.

Assuming you do all that, you then face the often-painful task of evicting the residents.

Now's the time to work on your end game — to implement your exit strategy. Although you shouldn't start rehabbing the property until the redemption period expires, you can't just sit around twiddling your thumbs until the redemption period expires and the homeowners move out. You have work to do. This chapter covers the all-important follow-through that secures your ownership of the property and provides a smoother transition from the previous owners to you.

Tying Up the Loose Ends after the Purchase

You probably spent a great deal of time and effort finding a property, researching it, and bidding on it or negotiating with the homeowners. You already have a considerable amount of money tied up in the property, as well, so you don't want to lose the property on some technicality or by overlooking a "minor" detail.

In the following sections, I show you what to do after you purchase a property to ensure that you've covered all your bases.

Closing on a pre-auction purchase

If you and the homeowners have a signed purchase agreement, the next step is to close on the property. At closing, you pay the homeowners, and they sign the title over to you. To make sure you don't get burned on closing day, make sure you're prepared:

- **Review the closing papers.** The title company should be able to provide you with a copy of the closing packet a few days prior to closing.
- **Call the utility companies.** To avoid getting socked with a high, unpaid utility bill, call the utility companies and ask for any account balances on service provided for the home. Let the utility companies know the date on which you plan to take possession of the house, so you don't have to pay for utilities you didn't use, such as electricity and gas. The water bill usually stays with the house or is tacked on to the property tax bill. Make sure you have the seller pay the water bill at or just prior to closing, so you don't get stuck with a huge bill.
- **Inspect the property.** The day before closing or even the same day, drive by the property to make sure the residents haven't trashed the place. If possible, knock on the door and try to get a peek inside. If you

can't get a peek inside, you may want to think twice about closing. You should have a relationship with the homeowners by now.

- **Verify title insurance.** Ask the title company for a letter verifying that the title is insured. Title insurance protects you from any unforeseen claims against the property.
- **Obtain homeowner's insurance.** Call your insurance agent and obtain an insurance policy for the property. If you're financing the purchase through a mortgage company, the company will want an insurance policy up front before closing. Purchase a one-year policy and bring a receipt to closing.

TIP

To trim the cost of insurance, consider increasing the deductible or insuring it only for the amount you have invested in it rather than for its replacement value. If you purchased a property for $150,000 and the house is worth $200,000, for example, you may consider taking out a $150,000 policy. If you're paying cash for the house or buying it with a commercial line of credit, this is one way to cut costs, but if you're financing through a mortgage company, you may be required to insure the property for the full replacement value of the property.

At closing, you simply sign the necessary papers as the closing agent or attorney sets them in front of you. Inspect the paperwork to make sure nothing has changed since the time you reviewed it. As soon as you've wrapped up all the paperwork, attend to these details:

- Obtain keys for the property.
- Call the utility companies to have the services transferred to your name.

TIP

A few days after closing, make sure the deed transferring ownership to your name has been recorded. If you're dealing with a title company, have it send or fax you a copy of the recorded deed. This copy will be date and time stamped and will bear the recoding information — the liber (book) and page number on which the deed was recorded, along with other information. If you're recording the deed yourself, ask the clerk for a copy that reflects the recording information. The office may take several weeks to officially record the deed, but the working copy is acceptable in the meantime. You may also be able to obtain a copy of the recorded document online.

Tying up the loose ends after the auction

After you purchase a property at auction, you escape the closing, but you may need to attend to other details, including fulfilling the conditions of the sale, obtaining title insurance, filing the deed, and insuring the property. Chapter 11 provides a complete checklist of everything you need to take care of after submitting the winning bid.

Protecting Your Investment through Redemption

In areas that have a mandatory redemption period, when you buy a property at auction, you become only "sort of the owner." Your name is on the sheriff's deed, but, depending on the rules and regulations that govern foreclosure in your area, the homeowners may have the right to redeem the property by paying back taxes and penalties and paying off all of their loans in full, complete with interest and penalties. The homeowners aren't likely to redeem the property, but if their rich Aunt Millie lends a hand, it could happen.

Your job as "sort of the owner" consists primarily of waiting for the redemption period to expire. During this temporary lull, however, you must continue to attend to your responsibilities as prospective owner. The following sections show you how to fulfill your obligations and guard your investment.

REMEMBER

The homeowners are not the only parties who can choose to redeem the property. Other lien holders can choose to redeem, and other investors may be able to work with the homeowner or buy out other lien holders and redeem your position. If you hold the senior lien, you can even sell your position to a junior lien holder, as explained in Chapter 19. Remain vigilant, and expect the unexpected.

Maintaining the property's status quo

Although the homeowners retain the right to reside in the property until the redemption period expires, insuring the property and paying the property taxes to protect your investment are pretty good ideas, even though they're not technically required. Here's what you should do:

- **Pay the property taxes.** The county treasurer sends you the tax bills. Simply pay them by the due date printed on the bill.
- **Take out an insurance policy on the home.** Without insurance, your entire investment is at risk of going up in flames, blowing away in a tornado or hurricane, or washing downstream in a flood. Make sure you're insurance agent knows that you purchased the property as an investment and will not be living in it.

  REMEMBER

  Finding an insurance agent who's willing to insure a foreclosure property is quite a challenge, but they're out there. The problems are that the insurance agent usually can't get inside to take photos, and you won't be living in the house. My insurance agent takes plenty of photos of the outside of the house and bases her quote on those photos and other details. You can expect a higher bill (perhaps even double the cost of owner-occupied homeowner's insurance), because the risk for the insurance company is higher. Just make sure you file an affidavit showing how much you paid, so you may be able to recover the expense if someone redeems the property.

- **File an affidavit for all expenses.** If your area has a redemption period, file an affidavit showing all expenses you paid for back taxes and homeowner's insurance. Your attorney can help you draft the affidavit and file it for you. If the homeowners or another lien holder redeems the property, you may be able to get this money back, but only if you file the proper paperwork when you pay the bills. (The rights to seek reimbursement for costs vary from state to state, so consult your real estate attorney for clarification.) File your affidavit the same day you pay the taxes, or the premiums; otherwise, you may be redeemed in the gap and lose you money.

Securing the property

If people are still living in the property, you have to rely on them for the most part to secure the property from theft and vandalism and prevent someone from getting accidentally injured. As owner, however, keep an eye on the property and attend to the following:

- **Lock the doors if the property is vacant.** Make sure the property is secure to prevent theft and vandalism and discourage neighborhood kids from entering the house or garage and possibly suffering some injury.

  TIP

  Consider giving your neighbors your card and asking them to keep an eye on the house for you. Ask them to call you if they notice anything out of the ordinary. If the house is vacant, you may want to hire one of the neighbor's kids to mow the lawn each week and pick up any newspapers or advertising handouts that end up on the front porch. Try to make the house look as occupied as possible.
- **Attend to any safety or health issues.** If the property has been cited for unsafe wiring, hire an electrician to inspect and correct the problem. Repair any broken windows or board them up. Invest a minimal amount of money to make the property safe. These are expenses you're highly unlikely to be reimbursed for in the event that someone redeems the property.
- **Perform any repairs that may lead to additional damage.** Spend only enough on repairs to prevent further damage. If the roof leaks, for example, instead of replacing the roof, have the leaks fixed to prevent further water damage.

Don't invest a great deal of money or time in expensive repairs. If someone redeems your lien, any money you spend now becomes a house-warming present to the new owners.

Keeping hungry investors at bay

A major threat to your investment property during the redemption period are other investors who may try to convince the homeowners that you're ripping them off. Another investor can step in, assist the homeowners with redeeming the property, and then buy it from them, cutting you out of the deal. Whatever you paid for the house at auction along with property taxes and insurance premiums you paid and filed an affidavit as having paid plus interest, are refunded to you upon redemption, but you lose the house.

You can't prevent the homeowners or someone else from redeeming the property, and you certainly can't prevent another investor from swooping in and bumping you out of a deal, but you can make it less likely. In the following sections, I provide tips for encouraging the homeowners to work with you toward a mutually beneficial conclusion.

Contacting the homeowners after the sale

As soon as possible after the auction, call the homeowners and let them know that you purchased their property. Tell them that other investors are likely to come knocking on their door or calling them to say that "so-and-so just bought your house and is going to kick you out." Explain that some of these other "investors" may try to convince (or con) them to do something that's not in their best interest, and that if they have any questions or concerns, they can call you.

Follow up with a letter that has all your contact information. I like to send one letter in the standard mail and one as a certified letter. Let the homeowners know that you're an investor, not a house stealer, and that you are willing to work with them if possible. For best results, send a letter immediately after the sale and then every six weeks or so until the redemption period has expired.

Offering cash for keys . . . and a nonredemption certificate

One of the best ways to keep other investors at bay is to visit the homeowners and offer them cash for keys and a signed nonredemption certificate. A nonredemption certificate is not a deed. You don't get the official deed until the redemption period expires, but it provides you with some additional assurance that you'll eventually get the property.

Consider giving only a small portion of the cash up front with the balance due after redemption and transfer of possession, so you're not out too much if something goes wrong and the homeowners have an incentive to honor the agreement.

Acting with integrity

Some foreclosure investors pay no attention to the homeowners' redemption rights. We had an investor in Oakland County, Michigan who was infamous for walking all over distressed homeowners. He'd buy a property at the sheriff's sale and immediately call the homeowners or knock on their door to tell them that he had purchased the property and they needed to vacate the premises immediately. He knew full well that the homeowners had six months to redeem, and he flat-out lied to them. More often than not, it worked — the homeowners immediately packed up and moved out.

I often use the dishonesty of other investors as a tool to bump them out of their deals. Knowing that a dishonest investor purchased a property at auction, I show up at the homeowners' door and say something like, "I noticed that so-and-so purchased your property at the sheriff's auction the other day. Did he inform you that you have six months to redeem the property before you have to move?" Of course, they say, "No," and then I can present them with a better offer.

I also do this when I see a property with an overbid — a bid amount in excess of what's owed on the property. The overbid money rightfully belongs to the homeowners. I'll say something like, "I noticed that so-and-so purchased your property at the sheriff's sale the other day. Did he tell you that the property drew an overbid and you're entitled to some of the money from the sale?" This provides me with another opportunity to work out a deal with the homeowners.

Some con artists make a living off of overbids. They attend auctions, note the properties that draw overbids, and then contact the homeowners and charge them 50 percent of the overbid to "help" them recover the money. All they're doing is stealing 50 percent of the money that rightfully belongs to the homeowners.

You may choose not to bump other investors from deals, but whatever you do, don't try to con the homeowners out of what is rightfully theirs. Let them know about any redemption rights they have or overbid money that's theirs. Give the homeowners a hand, and you quickly find that the homeowners become much more cooperative and later willing to recommend you to others.

WARNING!

Don't offer cash for keys and a signed nonredemption certificate if other lien holders have a claim to the property during redemption. You may end up handing the homeowners a thousand bucks only to have another lien holder redeem you the following day. Anything you give the homeowner is at risk, so don't offer a whole lot.

Prior to contacting the homeowners and offering cash for keys and a nonredemption certificate, consult your attorney. In some areas, having the homeowners sign a nonredemption certificate relinquishing their rights may be considered unethical. Be very cautious when working with the homeowner during the redemption period. You don't want to be accused later of taking advantage of the homeowners while they were under duress. My rule of thumb is to have no contact with the homeowner during the final month of the redemption period.

Once you have a nonredemption certificate in hand, avoid problems by maintaining a positive relationship with the occupants. You can enforce the nonredemption certificate in court, but more importantly it gives you some leverage if the homeowner has second thoughts or another investor approaches them claiming to offer a "better deal." Simply reminding the homeowners that you paid them money (consideration) for the agreement is usually sufficient to rein them in.

If the house is really a good deal, and you want to enforce the contract, you can try, but judges often rule on emotion rather than law and side with the homeowners. You'll have to hire an attorney, file an appeal, and pay attorney fees and court costs. If you think it's worth the expense and hassle, go for it. If not, you may want to walk away.

I've only run into problems with homeowners changing their minds a couple of times. In one situation, another investor offered to give the homeowners $5,000 instead of the $2,000 I offered if they would sell to him and not honor my non-redemption certificate. I ended up giving them $4,000 and explaining that that guy was a bum and probably would have taken the deed and scammed them out of their house without any money. I explained that I had already invested thousands of dollars by purchasing the property at auction, and this guy was only a cheap imitation without any real ability to deliver on his promises. After all, if he could, he would have bid against me at the auction. The extra $2,000 was still less than what I would have spent on attorney fees had I taken the homeowners to court.

Be very cautious when working with the homeowner during the redemption period, especially in the last 30 days. You don't want to be accused later of taking advantage of the home owner while they were under duress. My rule of thumb is to have no contact with the homeowner during the final month of the redemption period.

Planning Repairs and Renovations

During the redemption period, you own a non-performing investment — an investment property that's not earning you any money. You realize your profit only upon selling the property or leasing it out. To expedite repairs and renovations and realize your profit sooner, start planning renovations and lining up contractors now. In Chapter 17, I provide additional details on renovating your property.

Never spend lots of money on a house you don't yet own or that doesn't have a clear title. If you invest a lot of money in renovations and the homeowners redeem the property, you can lose your entire investment. If the property requires some repair or preventive maintenance, to prevent costlier repairs later, then go ahead and make the repair, assuming the property is vacant or the homeowners give you permission.

Evicting the Residents when Time Runs Out

Eviction can be ugly, so my advice is to avoid it, if possible. Make the process of moving out as easy as possible. Following are some suggestions for assisting the homeowners move out:

- **Give 'em time.** In extenuating circumstances, such as the illness or death of a close family member, consider offering to extend the eviction deadline. Show the homeowners the court documents with the date on which they're required to move out. Ask them if that's acceptable. If it's not, work with them to agree on a date and sign a commitment that they are going to move out on that date. Don't let the homeowners take advantage of your kindness — I've had homeowners claim that 17 of their grandmothers have died, just so they could hold on to the house a little longer.
- **Give 'em money.** Homeowners who have just experienced foreclosure are usually strapped for cash. Consider offering them $1,000 payable on the agreed upon moving date, on the condition that the property is in good condition and "broom clean" on that date. Broom clean means no junk left behind — it doesn't mean shiny clean.
- **Give 'em a dumpster.** To enable the homeowners to de-junk the place, consider offering them a free trash dumpster prior to moving day in which they can toss their junk.
- **Give 'em a moving truck.** If the homeowners haven't the means to move, take away the excuse by hiring a moving truck for them. Specify the time the movers are going to show up and have the homeowners commit to being prepared to load their stuff. Call the homeowners a couple days prior to moving day to remind them.
- **Give 'em free storage.** Contact a local mini-storage complex and arrange to pre-pay a couple months of the storage fee. The homeowners can then move their belongings into storage and pick them up later after they've settled into their new residence.

TIP

Arguing at this point is counterproductive. The homeowner's emotions are probably running a little high at this point. Simply explain that you didn't create the problem and are willing to do anything reasonably possible to assist them in moving on with their lives and leaving this problem in the past.

Playing nice guy doesn't always work, in which case you need to proceed with Plan B — a formal eviction. Fortunately, the court can assist you, to keep the eviction legal and to distance you from what may be an ugly scene.

To initiate the eviction, head down to the county courthouse and file a *trespassing action* with the court. The court assigns you a court date, which in my area is about two weeks from the date of filing. You meet the homeowners in court, and unless they have a good legal reason for not moving out, the judge gives them ten days or so to move out. If they need extra time, they can say so at the hearing, and if the extension is reasonable, you can agree to it. If the homeowners request 30 days, agree and sign without debate. I usually take the opportunity to offer an added incentive — "Move out by the agreed-upon date, leave the property broom clean, and I'll pay you an extra $1,000." Now you have something in writing.

I recommend that you always hire an attorney who's experienced with evictions to handle these matters for you. When I first started out, I handled most of this myself to save money and quickly learned that my approach was actually costing me more money.

If the homeowners fail to move out by the agreed-upon date, you can then call the sheriff and have the homeowners forcibly evicted. The bailiff shows up with the sheriff; the homeowners and all of their stuff are moved out of the house; and the sheriff locks the homeowners out of the house.

When the homeowners receive an eviction notice, they often become enraged. They may beat the house up, steal the furnace, break windows, tear out the kitchen cabinets, or completely gut the place stealing everything. Your homeowner's policy may cover the damage, but you still have the headache of trying to put the pieces back together. Work with the homeowners as closely as possible to keep their emotions in check.

Worried about homeowners trashing the house before eviction? Then talk to your attorney about getting a TRO (temporary restraining order) or a preliminary injunction which bars the homeowners from "committing waste" on the property. A TRO or injunction may make them think twice about punishing you by vandalizing the property, because the TRO carries the weight of the court's "contempt powers." You may not need to go through the trouble of obtaining a TRO, but if the homeowners make an offhand comment about trashing the joint or you suspect that they might take such action, look into it as a way to protect your investment. Homeowners who threaten vandalism are often homeowners you can't work with, so call your attorney immediately to see if a TRO or injunction is appropriate.

Chapter 17

Repairing and Renovating Your Investment Property

In This Chapter

- Drawing up a renovation plan and budget
- Beautifying a property that's in pretty good shape
- Whipping kitchens and bathrooms into shape
- Adding value with new rooms and features

Acquiring a foreclosure property for a price significantly below market value is like taking the perfect backswing in golf — it's a necessary first step to ensuring a profitable investment, but it's not enough to land you on the green. Once you acquire a property, work on your forward swing and follow-through. You need to renovate the property without blowing your budget and do it as quickly as possible, so you can sell the house before holding costs bite a huge chunk out of your profit pie.

In this chapter, I reveal the overall strategy for repairing and renovating an investment property to get the most bang for your buck. I warn you against making the common mistake of over-improving the property and then present renovation strategies and tips for everything from quick, cosmetic makeovers to major reconstruction projects.

TIP

All home buyers want a nice, clean house in the price range they can afford with as few mechanical problems (plumbing, gas, electric, and heating) as possible. When buying and renovating houses, let these factors guide your renovation decisions.

Choosing a Renovation Strategy

Having a plan of attack in place when you purchase a property can significantly reduce your holding time (and costs) and provide the focus you need to score a quick profit. You basically have four strategies from which to choose:

- **Don't renovate:** Buy the property and then turn around and resell it to another investor. Many investors are quite successful in finding bargain properties and then reselling them for $15,000–$20,000 over all costs.
- **White box:** Take a good, ugly house, clean it inside and out, patch any holes, and paint over any ugly stains with Kilz. Make sure the mechanicals (heating, electricity, plumbing, and air conditioning) are in good working order and that the roof has several years of life left in it. Price the house slightly below market value and pass the savings onto the buyers, so they can decorate and perform cosmetic improvements to suit their tastes.

  REMEMBER: By "paint over any ugly stains with Kilz," I'm not suggesting that you try to cover up major defects. If you notice a leak or have problems with mold or mildew, deal with the cause and proceed with essential repairs. Kilz and paint are simply to freshen up the appearance.
- **Complete rehab:** Clean the house inside and out as you do with white boxing, but perform the cosmetic renovations, too, including applying a fresh coat of paint, laying new carpet, and bringing the kitchen and bath up to market standards. See "Giving Your Property a Quick Makeover," later in this chapter for details.
- **Value-add renovations:** Perform a complete rehab and then take it one step further by adding a valuable feature to the house, such as an extra bedroom or bath, a dormer, a deck, or maybe central air-conditioning. See, "Adding Valuable Features," later in this chapter for details.

WARNING! Illegal house flipping has given flipping a bad name. Many lenders are now closely scrutinizing any sales in which the seller has owned the property for less than one or two years. Keep all your receipts and a detailed journal of your renovations to prove that you improved a property sufficiently to justify the sales price.

Planning Repairs and Renovations

The key to making money on an investment property is to buy low and sell high. What trips up many novice investors is the mistaken notion that "sell high" means transforming a Quonset hut into the Taj Mahal. They take the right first step, buying the property below market value, but then they over-improve the property in an attempt to maximize their profit. They end up owning a property that's worth more than any reasonable buyer is willing to pay for it.

When budgeting for repairs and renovations, your goal is to spend enough to bring the property up to the market standard in your neighborhood. Nobody is going to pay $150,000 for a house in an area where the next best house is selling for $100,000.

In the following sections, I focus your attention on the essential no-brainer repairs you must make, assist you in identifying the renovations that bring the highest ROI (return on investment), and show you how to estimate your ROI, so you don't renovate your way out of a profit.

Calculating the return on your investment

The producers of those house-flipping TV shows like to show the cost of a renovation followed by the amount it boosted the property value and the total return on the investment. On one show, a $5,000 landscape job supposedly boosted the value of a property by $20,000! In the real world, the ROI is rarely so cut-and-dried. I'm not about to tell you that a new $30,000 kitchen is going to increase the value of a property by $50,000 or that a $15,000 bathroom remodel is likely to net you a profit of $15,000. It just doesn't work that way.

The renovation isn't adding value to the house — it simply brings the property's value in line with that of other properties in the neighborhood. In the real world, you discount the purchase price by enough to cover the cost of the renovation and provide you with a profit of at least 20 percent. If the kitchen needs a $20,000 update to bring the house up to snuff, for example, you subtract at least $24,000 from your maximum purchase price. If the bathroom needs a $10,000 facelift, you subtract at least $12,000 from your offer. In other words, you calculate the cost of renovations into your purchase price.

Some renovations do add real value to a property. Converting an attic into a third bedroom, for example, or adding a garage to a house that doesn't have one adds value to the property. It boosts the property into a higher price bracket. Are value-added renovations worth the expense? The answer to that question depends on your market. To determine whether a particular feature is worth the expense, consider the following:

- **Comparable properties:** Check the value of comparable properties that have the feature you plan to add. How much more are these properties selling for? If you plan on adding a third bedroom, for example, check the recent sales prices of three-bedroom homes against the value of the average two-bedroom model.
- **Market demand:** Visit open houses in your area to find out what buyers are currently looking for. You want to make your house competitive with

comparable houses in the same neighborhood. Find out how much extra buyers are willing to spend for a house with an additional feature your house is missing.

- **Cost:** Obtain estimates on how much you can expect to pay to add the feature to the property. Does the added feature boost the property value enough to justify the expense?

Search for properties that have a missing feature and then add the missing piece. Some investors specialize in adding a bedroom to two-bedroom houses or adding a bathroom or half bath to houses that have only one bathroom. Others may add central air-conditioning to houses that don't have it.

Roughing out your budget and schedule

How much you profit from the sale of the house often hinges on the cost of repairs and renovations. Overzealous flippers get burned when their visions for improving a house exceed their ability to pay for them. Whether you have $10,000 or $50,000 budgeted for repairs and renovations, decide early on how much of that money to set aside for each project. To establish a budget, follow these steps:

1. **List the projects you plan on hiring a professional to complete.**
2. **Obtain estimates for these jobs.** Estimates should break out the cost of materials and labor.
3. **Jot down the projects you plan on doing yourself.**
4. **For each of these projects, list the required materials.** If you're remodeling a bathroom, for example, you may need a new toilet, sink, cabinet, tile (for the walls), flooring, paint, and caulk. Visit your local hardware store to research the cost of materials.

   Many hardware stores display two prices for materials — an uninstalled and an installed price. Use these comparisons to determine how much you would save by doing the work yourself.
5. **Tally all the estimated costs and add 20 percent to cover sales tax and unexpected expenses.** The cost of most projects exceeds estimates.

Use the renovation planner shown in Figure 17-1 to estimate costs and keep all your notes in one place. The planner features space for listing each project, its start and completion dates, and costs for materials and labor.

The tentative budget provides you with a clear idea of whether the total costs of your planned projects are on track. If you do your homework before purchasing the property, your costs should be right on target to ensure a profit when you sell. If costs are running over budget, consider scaling back on nonessential projects.

Renovation Planner					
Project	Start Date	Completion Date	Materials Cost	Labor Cost	Total Cost

Total Materials Costs		$	______________
Total Labor Costs	+	$	______________
Total Materials and Labor Costs		$	______________
20 Percent for Sales Tax and Unexpected Costs	×		1.2
Grand Total		$	______________

Figure 17-1: A renovation planner is a handy tool for estimating costs and scheduling work.

WARNING!

Don't let some sweet-talking contractor charm you into taking on a project in which you're destined to overspend. When budgeting, make sure that you're the one making the decisions on how to spend your money.

For additional tips on renovating a property and preparing it for sale, check out `www.HurryHome.com`.

Giving Your Property a Quick Makeover

You bought a good, solid home in a decent neighborhood for well below market value. The house needs no major renovations, but the previous owners failed to update and properly maintain the property. You now are the proud owner of an ugly house — the perfect candidate for a quick and affordable makeover.

For a few thousand dollars over the course of a few days or weeks, you can polish that diamond in the rough into a jewel that's well worth full market value. In the following sections, I step you through the process of renovating a decent property on the cheap.

TIP

Your goal with most renovations is to fix anything that distracts from the rest of the house. You don't want prospective buyers to walk out because something doesn't look right or smell right. You don't want them offering you $20,000 less than your asking price because the house needs a $10,000 repair job. If you can't picture your spouse happily living in the house, it probably needs something.

Freshen the exterior

Curb appeal is the number-one area of focus for home buyers. If the property is ugly on the outside, prospective buyers will never step through the front door to peek inside. To quickly freshen the exterior of the property, here's what you do:

- Trim tree limbs and shrubs.
- Mow and edge the lawn.
- Replace dead or dying shrubs and plant flowers, in season, of course, and especially near the front.
- Apply a fresh layer of mulch.
- Remove clutter and eyesores.
- Fill driveway and walkway cracks.

- Power-wash the siding, tuck-point a brick home (add fresh mortar between the bricks), or paint a wood-sided home.
- Remove any window air conditioning units.
- Repair or replace windows and screens.
- Add or replace shutters.
- Paint the front door and trim.
- Paint the garage door, the front door and shutters all the same color to match the house.
- Replace the gutters. Seamless gutters are best.
- Replace the front and rear storm doors.
- Replace exterior light fixtures.
- Replace the mailbox with something classy that matches the exterior style of the house.

Gussy up the interior

Foreclosure properties are usually neglected, particularly inside, where the neighbors can't see. Every room in the house is likely to require a little tender loving care, which you can provide by doing the following:

- Give the place a good scrubbing.
- Wash the windows.
- Install new window blinds.
- Clean or replace any drapes or curtains.
- Remove hooks or nails from all walls and patch the holes.
- Apply a fresh coat of paint to all rooms using flat, neutral colors and semi-gloss white for the trim.
- Check and repair all doors and doorknobs. Doors should open and close effortlessly.
- Install new light switch and outlet cover plates.
- Install new smoke detectors.
- Re-carpet, refinish, or replace damaged or worn flooring.
- Swap out the register covers.
- Replace exhaust fan covers and maybe the fans.

Tidy up the kitchen

You don't have to gut the kitchen to make it look shiny and new. The following affordable solutions often do the trick:

- Install a new stainless steel sink.
- Install a new faucet.
- If the countertop looks old or crusty, have it replaced.
- Refinish the cabinets, if needed, and add new hardware — knobs and handles.
- Apply new contact paper to all cabinet shelves and drawers.

Scour the bathrooms

Bathrooms in foreclosure properties often look like the inside of a neglected fish tank. If a thorough scrubbing won't do the trick, consider the following affordable renovations:

- Install a new vanity.
- Install all new fixtures.
- Replace the toilet seat.
- Replace old towel hangers.
- Replace shower curtains or install glass shower doors.
- Apply a fresh bead of calk around the edges and base of the tub or shower, around the sink, and around the base of the toilet.
- Scrub the grout between any tile work thoroughly.

TIP

Some companies, often referred to as grout doctors, specialize in cleaning out the mold and mildew between tile or even re-grouting it or re-glazing it and making it look shiny new without having to replace the tile. The investment is well worth the money, and it rarely costs as much as most people assume. If the bathtub looks bad, consider having it re-glazed, as well.

Spiff up the bedrooms

Assuming you already painted and re-carpeted the entire house, you've pretty much done all you need to do to the bedrooms:

- Paint.
- Re-carpet.

- Replace light fixtures, cover plates, and heat register covers.
- Install closet organizers, if needed.

Make the basement tolerable

Converting the basement into an extra living room, bedroom, rec room, or personal gym, is rarely a smart investment. Focus your efforts on making the basement a clean storage or utility area:

- Sweep the cobwebs out of the rafters.
- Dust any ductwork, pipes, or wiring (be careful around the wiring).
- Tack up any dangling cables without shocking yourself.
- Seal all cracks in the walls.
- Whitewash concrete or cement-block walls with a sealing paint. (If the basement smells musty, scrub with a bleach solution before painting. You can also run a dehumidifier in the basement, but run the overflow hose to a floor drain, so you don't create the appearance of standing water in the basement.)
- Paint the concrete floor using gray enamel paint or tile the floor.
- Install new glass block windows.
- Buy a roll of insulation and stuff pieces of it between the joists where the joists meet the outside wall. Painting the joists a darker color often adds a nice, clean touch.

TIP

Unless a basement has its own entryway to the great outdoors, you can't consider it official "living space." Novice investors often try converting basements into living space, but when you list the house, it's officially a basement and does not figure into the square footage calculations.

Attend to the mechanicals

Everything in the house should function properly and look its best, including the water heater, furnace, air-conditioning unit, and plumbing:

- Change the furnace filters.
- Clean or replace the hot water tank.
- Repair any leaky faucets.
- Unclog any plugged or slow drains.

Investing in High-Profile Rooms: Kitchens and Baths

Kitchens and bathrooms sell houses, so don't overlook or underestimate the need to transform these high-profile living spaces into attractive and highly functional rooms. In the following sections, I suggest some kitchen and bathroom renovations that range from affordable updates to pricey upgrades.

Cooking up a remodeled kitchen

Starting at about $15,000, you can completely gut an average kitchen and install new mid-level cabinets, countertop, sink, and dishwasher. For a few thousand more, you can kick in a new range, stovetop, microwave oven, and refrigerator. You don't have to spend that kind of money updating the kitchen, and you can spend a lot more than that. In the following sections, I take you on a tour of kitchen upgrades starting with cost-cutter rehabs and moving up the ladder.

Giving the kitchen an affordable facelift

You can give the kitchen a whole new look with a few very affordable updates:

- **Refinish the cabinets.** Paint the cabinets white, strip and re-stain, or reface the cabinets. Re-facing consists of removing the doors and the fronts of the drawers and then applying a wood or plastic laminate to all exterior surfaces. This re-facing is much more expensive than a standard paint job, but it costs about a third less than installing new cabinets, and it usually looks just as good.
- **Replace the cabinet doors.** If the cabinets are solid, refinishing the cabinets and replacing only the doors is always an option.
- **Replace the drawer knobs and cabinet handles.** For a few bucks per drawer or door, you give the cabinets a whole new look.
- **Polish or replace the countertop.** For a few hundred dollars, you can hire someone to polish a solid countertop, such as marble, granite, or a composite material to buff out the dings and scratches. If the counter is laminate, replace it.
- **Install a new sink and faucet.** For a couple hundred bucks, a new sink and faucet make the entire kitchen look cleaner and more modern.
- **Lay new flooring.** In most older kitchens, the floor looks bad no matter how clean it is. To make it look brand new, install new flooring — ceramic (high-end) or vinyl or linoleum (lower- to mid-range markets).

For more about redoing a kitchen, check out *Kitchen Remodeling For Dummies* by Donald R. Prestly (Wiley).

Gutting the kitchen

Some kitchens are hopeless. The cabinets are shot, the countertop is age weary, the sink is beyond salvation, or the kitchen is simply too dinky to comfortably accommodate the average family. When a kitchen sinks to this level, consider gutting it and starting over.

I don't recommend that you redesign a kitchen on your own. Head down to the local cabinet or building supply store and consult with a professional kitchen designer. If you're planning on knocking out a wall or two to expand the kitchen, you should also consult with a builder or engineer, so you don't accidentally demolish a wall that's supporting the roof or the second story.

You can save yourself some money on a kitchen remodel by doing the tear-out yourself or hiring some unskilled laborers to do it for you. Even if you're very careful, you can complete the tear-out operation in less than a day. You're then ready to call in the installation crew to mount the cabinets, install the countertop, lay new flooring, and fit the rest of the pieces in place.

Modernizing kitchen appliances

Chances are pretty good that the distressed homeowners took their kitchen appliances with them or the ones they left behind are pretty shabby. In a high-end market, buyers are likely to want to pick out their own appliances. In a low- to mid-range market, however, having clean, functional appliances in place is a big plus.

Before you shell out $10,000 or more for top-of-the-line appliances, take a deep breath and a look around at the housing market in your area, and let your market guide your choices:

- In low- to mid-range housing, supply the bare essentials — a dishwasher, garbage disposal, refrigerator/freezer, and freestanding range.
- In mid- to upper-end housing, consider supplying the higher-end essentials along with a cabinet with warming drawers and a built-in wine cooler. Upgrade to a built-in refrigerator with an ice maker and water dispenser, and consider upgrading the oven and cooking surfaces, and possibly adding a trash compactor.
- In any market, replace the old microwave with a new, space-saving, over the counter model. Counter space is golden — free up as much counter space as possible.

If you purchased a house without a dishwasher, add one, even if it involves losing a little cabinet space. You can pick up a standard dishwasher for as little as $200. If the kitchen already has a dishwasher, installation runs about $100, and the installer usually hauls away the old unit for $25 or so. Expect a first-time installation (for a kitchen that doesn't have a dishwasher) to cost another $100 or more for the plumbing installation.

Adding Valuable Features

In most of the foreclosure properties I renovate, I rarely add value-boosters. I buy the house below market value, renovate as needed to bring the house in line with market value, and sell it. I do, however, stumble across the rare property that has the potential to jump from one price bracket to the next. A small home that's nestled in an area with much larger homes, for example, may be a prime candidate for expansion.

When you're planning renovations, look for any opportunity to boost the property into a higher price bracket by adding valuable features that other homes in the area already have. Following are some ideas to get your creative juices flowing:

- Replace the windows
- Replace the doors
- Add central air-conditioning, if missing
- Open up the floor plan
- Raise the roof
- Add a deck or patio
- Convert underused spaces into living spaces
- Add a bathroom
- Add a bedroom
- Build a garage

Don't go too crazy modifying the floor plan or converting unused space into living quarters. I once purchased a house in which the previous owner converted the garage into a den. The house had no garage, and the lot had no space for one, so the first thing I did was convert the den back into a garage. When renovating, follow the Hippocratic oath: First, do no harm. Sometimes the less you do, the better.

Chapter 18

Cashing Out: Selling or Leasing Your Property

In This Chapter

- Selling quick and for top dollar through an agent
- Primping your property for a showing
- Marketing your property to spark interest
- Negotiating offers and closing the deal
- Leasing your property for steady cash flow

Most investors who deal in foreclosures flip properties — they buy the property at a bargain price, repair or renovate it if necessary to maximize their return on investment, and then turn around and place the property back on the market. Some investors, however, prefer the buy-and-hold strategy — leasing the property for a steady cash flow.

In this chapter, I cover both strategies. If you decide to sell, I steer you clear of the common mistake of trying to sell the home yourself to avoid paying a sales commission to an agent. I reveal strategies and tips for pricing the property to sell and sprucing it up so it sells faster at a higher price. You also discover some high-power marketing strategies to generate interest in the property and savvy negotiating maneuvers to obtain the best price without haggling yourself out of a sale.

For those of you who are practicing the buy-and-hold strategy, I suggest some of the pros and cons of leasing the property and taking on the role of landlord, which many investors are simply not cut out to do.

Sell it yourself?

Sellers often try to sell their homes on their own to avoid paying an agent commission, but it rarely saves them enough to justify the hassle. What usually happens is that when a buyer shows up to place an offer on the house, the buyer knows that the seller is saving about 6 percent by listing the home themselves. So, the buyer automatically deducts an additional 6 percent from his offer. If the sellers accept that offer, they essentially give the buyer as much as they would have paid the agent, and the sellers had to do all the work without the additional benefits of having professional assistance and advice!

Most people choose to sell without an agent because they've had a bad experience with a real estate agent or felt that the agent didn't do enough to justify his six percent commission. This is a very valid point, but it simply means that the seller didn't pick the right agent.

When selling a house, don't just look at the cost of hiring an agent. Look at the cost of not hiring an agent and consider the benefits that an agent brings to the table . . . particularly the closing table.

Selling Through a Qualified Real Estate Agent

You can boost your bottom line on a property in two ways — increase the price or cut expenses. Increasing the price, as discussed later in the section is often counterproductive, as discussed in "Generating Interest Through Savvy Marketing," later in this chapter. Cutting expenses, within reason, may be a possibility, but steer clear of any temptation to cut costs by trying to sell the house yourself. Why? In the following sections, I answer that question and then provide tips on how to select an agent who's best qualified to sell your property.

Selling faster for a higher price

Sure, a 6–8 percent agent commission can take a sizeable bite out of your net profit, but consider the advantages of having an agent:

- On average, an agent sells a home in half the time it takes a homeowner working alone. If you ballpark your holding costs at $100 per day, you lose about $3,000 every month your property sits on the market.
- According to the NAR (National Association of Realtors), the average home sells for 16 percent more when sold by a Realtor. A Realtor is a

real estate agent who's certified by the National Association of Realtors and is required to receive additional training and adhere to a strict code of ethics.

- An agent can market to other agents through her access to the MLS (Multiple Listing Services) and by networking with other agents, relocation firms, and other services to increase interest in your property and possibly even start a bidding war that can boost the sales price.
- An agent can pre-screen buyers, so you don't waste time showing the home to people who don't have the cash and can't obtain the financing to buy it. You want qualified buyers, not lookie-loos.
- An agent takes on the burden of fielding phone calls from interested buyers, scheduling tours, showing the house, and handling the paperwork. That's time you can spend working on other investment properties.
- Having an agent during negotiations is like putting on a poker face when playing cards. The agent can negotiate with a buyer without giving away any secrets concerning what you may be willing to accept.

TIP

I recommend that you sell the property yourself only if the conditions are right:

- Someone walks through while you're rehabbing and is willing to sign a purchase agreement on the spot, and you completely understand the purchase agreement and are confident in executing the agreement without the assistance of a professional.
- You're in a seller's market — an area where you have significantly more buyers than sellers. Try this only for a short period of time. If the house doesn't sell, call an agent.
- The house is on a street that already has plenty of buyer traffic, and you have the best house with the best price. (Of course, if you follow my guidance in Chapter 17, you should always have the best house at the best price.)
- You have the time and desire to show the house at any time of day or night when a buyer calls to see it.
- You have the computer skills required to produce slick marketing materials and advertise on the Internet.
- You're able to show the house without tipping your hand.
- You intend to hire an attorney to approve all the documentation and attend the closing.

In the following sections, I offer guidance on finding an agent who's best qualified to sell the property.

TIP

If you're trying to sell the home yourself, plant an FSBO (for sale by owner) sign in the front yard along with a note saying something like "Buyer's Agents Welcome" or "Commission Paid to Broker." This lets buyers agents know that if they show the home to someone who purchases it, you're willing to pay them something. This may increase traffic.

Choosing a top-notch seller's agent

Real estate agents generally fall into two camps: buyer's agents and seller's agents (also called *listing agents*). Think of the difference in terms of prosecuting and defense attorneys. Each type of attorney specializes in serving a different type of client with very different needs.

In real estate, a buyer's agent is typically much more skilled in looking out for the interests of the buyer — finding the right house for the buyer at the right price and negotiating for a lower price and more attractive terms. A seller's agent has a skill set that leans more toward marketing and sales. (Some top-producing agents have a team with both buyer and selling agents. These are the cream of the crop.) For a seller like you, a seller's agent offers the following unique benefits:

- Price your house to sell for top dollar without lingering on the market.
- Market your property more effectively — a buyer's agent may be less skilled at marketing.
- Ensure that you properly disclose any defects in the property.
- Pass along any information about the buyer that may assist you in negotiating for a higher price.

To choose a qualified real estate agent, make sure the agent has the following credentials, experience, and drive:

- **Credentials:** Designation or certification proving that the agent received proper training, such as CRI (Certified Residential Specialist), GRI (Graduate Realtor Institute), StarPower Star or member, or Golden R-Top 1% Club.
- **Experience:** Ten years or more of experience. You may find an inexperienced agent who's very well qualified, but an experienced agent with a solid track recorder is more of a sure thing.
- **Drive:** Choose an agent who does her homework and can provide you with market analysis and listings of comparable properties. The agent should be willing to hold open houses, show the house on a moment's notice, and be attentive to your questions and needs.

REMEMBER

For assistance in finding a qualified real estate agent who can sell your investment property for you, visit www.GuthyRenkerHome.com and click the tab for sellers. You can then register and have real estate agents call you, instead of having to search for a qualified agent.

Staging Your House for a Successful Showing

Staging a property consists of making it look as pretty as possible. Studies by the staging industry (yes, you can hire professionals to stage your home) prove that a properly staged home sells in half the time for 7–10 percent more than a comparable un-staged home. Given those numbers, a home that would normally take three months to sell at a price of $250,000 would sell in six weeks for $267,500 to $275,000 with professional staging!

Of course, you're free to hire a professional stager, but if your budget is already strained, you can probably do a pretty good job staging the home yourself. In *Flipping Houses For Dummies* (Wiley), I devote an entire chapter to the basics. In the following sections, I provide a brief overview of the areas to focus on when staging the house you're selling.

Jazzing up the front entrance

During your renovations, you improve the appearance of the house so much that minor imperfections stick out. Carefully inspect the outside of the house for anything that sticks out, and attend to it immediately. Here are some tips for perking up the curb appeal:

- **Spruce up the landscaping.** Mow and edge the lawn, pull weeds, fix any cracks in the pavement, and sweep up after yourself. Lay fresh mulch and plant fresh flowers (if in season) and keep them watered. While you're at it, put the garden hose away and hide the garden gnomes.
- **Freshen up the entryways.** Sweep the porch and stairs, lay down an attractive new doormat, fix the screens, wash the windows, polish the doorknobs, and clear the clutter out of the entryways. Make sure the doors open and close with ease.
- **Check the outside lights.** Make sure the porch and security lights are working.

Decluttering the joint

Clutter makes a house feel cramped and makes buyers nervous. Investment properties usually don't have a problem with clutter. You probably de-junked the place before you started repairs and renovations, but if you can't walk through the house without tripping over something, then take the following steps to remove non-essential items:

- **De-junk the joint.** Remove all non-essential items. You can sell the stuff, dump it, or give it away. Just make sure it doesn't appear on the premises.
- **Clear the counters.** Counter space is pure gold. In the kitchen, remove everything from the counters including coffee pots, electric can openers, blenders, toasters, flour tins, cookie jars, and especially knife racks and dish drainers. In the bathroom, hide the toothbrush holder, hair brushes, lotions and creams, and other glamour paraphernalia.
- **Empty the closets.** Storage space is prime real estate.
- **Ditch politically incorrect décor.** A house showing is an emotional event. Any décor that may stir negative emotions in potential buyers has to go, including religious icons, political paraphernalia, and zodiac signs.

Adding a few tasteful furnishings

When showing a house, your goal is to create a blank canvas on which buyers can paint their dreams and visions. Less is more, but a vacant house can be just as unappealing. Homeowners want to be able to envision themselves living in the house, so make it look livable with a few tasteful furnishings:

- A small kitchen or dining room table with matching chairs. Dress the table with an attractive tablecloth (not plastic), a bouquet of fresh-cut flowers, or some other attractive centerpiece. Better yet, opt for a table with a glass top — it can make the kitchen look a little roomier.
- An attractive sofa and a coffee table in the living room or den. Accent the room with a few small lamps and a bit of greenery. Hanging some nice, simple mirrors that reflect the windows can also create the illusion of wide-open space.
- A standard-sized bed and small dresser in the master bedroom.
- A few neutral paintings or other artwork on the walls.

Seasoned investors often have some nice surplus furniture left behind in other homes they've sold. To keep costs down, consider moving some furniture from your permanent residence to the house you're selling or borrowing surplus furniture from friends or family members.

To gather some ideas on how to professionally stage a home, visit a few model homes in newly constructed subdivisions. You quickly notice that these model homes are clean, tastefully furnished, and attractively decorated. They're never vacant. Also check out the window dressings. In models, instead of heavy curtains or blinds, you typically see something more airy, like valances.

Appealing to the senses

When you go out to eat at a fine restaurant, the quality of your dining experience relies on much more than the quality of the food and service. The lighting, aromas, and background music all contribute to the ambience. When staging a home, you want to create a pleasant sensory experience for the buyer. Following are some tips to assist you:

- **Light it up.** Turn on all the lights to make the house appear warmer and roomier and prove that you're not trying to hide something.
- **Bring the outside in.** If the weather's nice, open up the house to air it out. Add fresh cut flowers to the kitchen, living room, and den to add a fresh, natural aroma. Most professional homeowners recommend against using potpourri, scented candles, and air fresheners. If the home has a fireplace, consider lighting it . . . only in season, of course. Another nice touch is to arrange cut and uncut citrus fruit in a glass bowl on the kitchen counter or dining room table — the natural aroma of fresh citrus is pleasant without being overpowering and the arrangement is both attractive and inexpensive.
- **Play some relaxing background music.** Classical music is often a good choice. Rock, rap, and heavy metal are usually bad choices.

If you're living in the house you're selling, you may be tempted to hang out while your agent shows the prospective buyers around. Avoid the temptation. Your presence can make the buyers nervous and make the house feel crowded. Step out until everyone leaves. You can contact your agent after the showing to find out how it went.

Generating Interest Through Savvy Marketing

If you took my advice and hired a top-notch seller's agent to list your property, she can handle the marketing for you, primarily by creating an MLS listing. If you decide to sell the home on your own, the marketing job falls on your shoulders, and without access to the MLS, you have to ramp up your marketing efforts. Here are some ideas on how to create your own effective marketing campaign:

- **Set a competitive asking price.** Shoppers look for value. Set the right asking price, and you attract more buyers. Set your asking price too high, and the property is likely to linger on the market while holding costs chip away at your profit. Set the price too low, and prospective buyers may think there's something wrong with the house. Starting a little high is preferable to starting a little low — you can adjust down, but adjusting up can raise some eyebrows. Smart agents and buyers ask for a listing history.
- **Plant a For Sale sign on the front lawn.** The For Sale sign taps into "the power of 20" — the five neighbors on either side of you and the ten neighbors across the street immediately notice the sign and start telling people about it. Use a professional sign, not one of those cheap, wire-frame jobs they sell at the local hardware store.
- **List the property online.** Several companies list homes for sale by owner, where buyers can search for homes without going through an agent. Before you sign up with one of these services, make sure that it's legitimate, that it lists plenty of homes in your area, and that it's used by many buyers in your area.
- **Advertise in the classifieds.** Post an ad in the classified section of your local newspaper and on any classifieds sites, such as Craig's list (at `sfbay.craigslist.org`) and Backpage (at `www.backpage.com`).
- **Design, print, and distribute flashy fliers.** Include full-color photos of the property highlighting its most attractive features. Also include the address of the property, the asking price, a description of the property, your name, and your phone number. Print the fliers on high-quality paper and post them wherever you can legally do so — grocery stores, gas stations, restaurants, and apartment complexes, to name a few.
- **Design, print, and distribute business cards.** Create a business card for the house and pass it out to everyone you meet.
- **Generate some word-of-mouth buzz.** Soon after placing the house on the market, host an open house and invite the neighbors. Post some Open House signs around the neighborhood and provide food and beverages. Sunday afternoons are usually the best times to schedule an open house, because people have nothing better to do.

TIP

To effectively market any product, determine who's likely to buy it. When marketing a house to a first-time homeowner, for example, you may highlight the affordability of the house and provide a lead on where to go for financing. When marketing to movin'-on-up buyers, you may want to pitch the house as being spacious beyond belief. Empty-nesters and down-sizers are often looking for something smaller that's in move-in condition. Consider sending flyers to the residents of local apartment complexes. Modify your marketing materials to appeal to your target buyers.

Negotiating Offers and Counteroffers

When prospective buyers deem your house worthy of purchase, they present an offer, in writing, of the price and terms. The high-profile part of the offer is the purchase price, but savvy sellers don't focus on price alone. They consider the *price and terms* of the offer. In many cases, a lower offer is superior if the buyer has the cash or financing in place and doesn't demand a lot of extras, such as closing costs and repairs.

In the following sections, I provide some guidance on how to pick the best offer from two or more competing offers and show you how to negotiate to get more of what you want.

Comparing offers

When you're buying and selling houses, you need to be able to evaluate offers based on the following factors:

- **Price:** An obvious lowball offer may cause some concern, but if you set your asking price in line with comparable properties, the offer should include a price that's pretty close to your asking price. I usually consider a cash offer of 5 percent below my asking price pretty good, and I expect a higher offer if the buyer needs to finance the purchase.
- **Buyer's financing:** Cash is King, pre-approved financing is Queen, and pre-qualification is a Jack. An offer that proves the ability of the buyer to close on the sale is much better than an offer from buyers who plan on applying for a loan after they find the house they want. If you have any doubts about a buyer's financing, ask them to contact your mortgage specialist (loan officer), who can then advise you on the buyers' ability to qualify for financing.
- **Earnest money:** The more earnest money a buyer includes with the purchase offer, the more likely the buyer is willing and able to purchase the property. An earnest money deposit of at least 1 percent of the purchase price shows a fairly strong buyer commitment.
- **Conditional clauses:** Standard conditions include that the property must appraise at the sales price or higher, title must be clear, and the house must pass inspection. Watch out for anything that can undermine the closing, including conditions that the buyer's existing home must sell first. Contingencies that allow the buyer to back out of the deal without just cause (commonly called *weasel clauses*) also raise red flags, such as "buyer's attorney must review and approve the offer."
- **Closing date:** A faster closing reduces your holding costs, so if one buyer offers $2,000 less than another buyer but can close a month earlier, the lower offer may be the better offer.

Steering clear of cash back at closing deals

More and more buyers are looking to get a little cash back at the closing table. They may even offer to pay more than your asking price with the agreement that you will hand the excess cash back to them at closing. Cash back at closing deals are illegal, no matter what the buyer claims to need the money for—repairs, renovations, to pay off credit cards or medical bills, whatever.

Why are these deals illegal? Because the lender is never "in the know." To obtain cash back at closing, the buyer must fool the lender into thinking that the house is worth as much as the buyer is asking to borrow. The lender approves the loan thinking that the home's value is sufficient to cover the loan amount — if the borrower can't pay the mortgage, the bank can foreclose and sell the house to cover the loss. Cash back at closing deals trick lenders into approving riskier loans.

If someone approaches you with a cash back deal, call the lender. The lender's phone number is usually listed on the mortgage note or the closing instruction letter included in the closing papers.

Accept offers only from serious buyers who are at least pre-qualified for a loan that's sufficient for purchasing your house. Have your mortgage specialist on call to check up on a prospective buyer's qualifications before you sign the purchase agreement. Your mortgage specialist can contact the buyer's lender and perform background checks to ensure that the buyer has sufficient financing in place.

REMEMBER

If you're not 100 percent confident in a buyer's offer, consider countering the offer with a 72-hour contingency. This allows you to accept the buyer's offer while continuing to market the property. Your agent should be well versed in this strategy.

Mastering the art of counteroffers

Some offers are so low, all you can do is laugh and shrug them off, but in most cases, no offer is too low to reject outright. When you receive an offer that appears to be a little irrational, don't take it personally. If you're not ready to say either "yes" or "no," simply reply with your counteroffer.

To more effectively navigate counteroffer negotiations, employ the following strategies and tips:

- Pitch the counteroffer through your agent. Otherwise, you risk tipping your hand.
- Make yourself readily available to your agent during the negotiation process, so you can quickly respond to counteroffers.

- Don't bid against yourself. Wait for the buyer's counteroffer before offering any additional concessions.
- Don't give ultimatums. Ultimatums or take-it-or-leave-it offers shut down communications. Successful negotiations require an open forum.
- Don't let a personality clash get in the way of making the deal.
- Keep a lid on it. If you talk too much, you're liable to tip your hand or upset the buyer, neither of which is productive.
- Respond only in writing. If the buyers or their agent contact you over the phone with a proposed offer, request that they present it in writing to keep it legal. In real estate, everything has to be in writing to be legal.

If you receive an offer that is pretty close to what you want, you don't have to counter. If you can live with the offer, countering a couple thousand dollars higher may be a bad idea, and it generally is. It lets the buyer off the hook and free to pursue the search for another house. If you are getting lots of offers, then you may want to counter, but in a buyer's market, an offer that's close to what you want, with acceptable terms, may just be a great offer.

TIP

Consider countering a low-ball offer with a high-ball offer. If the buyer offers $100,000 on a house you listed for $143,000, consider countering with $142,500. This lets the buyer know that you'll deal, but they have to be serious. Have your agent contact the buyer's agent and try to feel them out why the offer was so low. Have your agent "play the game" — tell them that the sell has some wiggle room, but not that much. Your agent may say she convinced you not to just completely reject the offer but to try to work with this buyer. This may build some good will with the buyer that may result in a more reasonable offer. Your other option is to simply write "Rejected" across the offer and send it back to them.

Closing the Deal

After you and the buyers reach an agreement on price and terms, and assuming nothing happens to sabotage the deal, the sale proceeds to closing, where you receive your money and sign over the deed to the buyer. At this point, you have two goals — to make the closing proceed as smoothly as possible and to ensure that your back end is covered.

REMEMBER

As soon as you and the buyer agree on price and terms, return the documents to the buyer's mortgage company and to your title company or real estate attorney and schedule a closing date. Closings typically occur 30 to 45 days from the day you sell the property, so you don't want to waste any time. As soon as you sell the property, you must order the title policy, the mortgage commitment. Neither the buyer nor seller need to worry about this — your real estate agent keeps the process moving forward and can recommend a title company or attorney to handle the paperwork.

To ensure that the closing proceeds as smoothly as possible, supply your closing agent with any documents she may need to put together the closing packets. Documents typically include the following:

- Termite inspection report. If the buyer is receiving FHA (Federal Housing Administration) financing to purchase the house, immediately schedule a termite inspection and send the report to the closing agent or attorney who's handling the closing.
- Purchase agreement and any addendums.
- Mortgage payoff information and any second mortgages or other liens.

WARNING!

Even if you sell the house yourself, you should have professional representation at the closing — a qualified Realtor or a real estate attorney. Remember that Realtors are not lawyers and cannot give legal advice. Obtain the closing packet two or three days prior to closing, review the papers with the assistance of your attorney or Realtor, and clear up any issues and concerns prior to closing time. Get your attorney involved before you sign on the dotted line. After you sign, your attorney has much less power to protect you.

Becoming a Landlord

Most people who invest in real estate are looking for a quick score. They buy, sell, and then sit back and count the money. Others prefer the buy-and-hold strategy, renting out the property for some period of time before selling it. The buy-and hold strategy offers several valuable benefits:

- By holding the property for one year and a day, you pay long-term rather than short-term capital gains on your profit. During the writing of this book the feds were charging 35 percent in short-term capital gains and only 15 percent in long-term capital gains.
- You can claim depreciation of the property as a tax deduction. This is a rare tax situation in which you can claim depreciation as the property appreciates.
- You profit in three ways — you profit when you buy the property below market value, the property appreciates over time, and the rent from your tenants pays down the principle on the loan.
- You can deduct any expenses you incur for the maintenance and management of the property.

These tips are simply suggestions on strategies to discuss with your accountant.

Keep in mind that not everyone is landlord material. You have to find renters, collect the rent, maintain the property, and be able to handle calls from tenants at any time of the day or night. You may be able to hire a property management company to take care of all this for you, but that can cut into your profits. If you're considering the leasing option, I strongly recommend that you read *Property Management For Dummies* by Robert S. Griswold (Wiley).

Chapter 19

Checking Out Other Cash-Out Strategies

In This Chapter

- Cashing out the equity in your property
- Selling the house back to the previous owners
- Renting the property to the previous owners
- Offering a rent-to-own agreement
- Selling your senior lien to a junior lien holder

Buying a foreclosure property, fixing it up (or not), and then placing it back on the market is the most common way to profit from your foreclosure, but it's not the only way. You can instantly profit from your property by refinancing your loan for more than you've invested in the property, or you can sell or lease the property back to the previous owners, or even sell the senior mortgage you bought at auction to another lien holder.

In this chapter, I reveal several strategies to pull the equity out of your property along with other novel ways to profit from your foreclosure investment.

Refinancing to Cash Out the Equity

Homeowners commonly refinance their homes to cash out equity. Refinancing consists of simply taking out a new mortgage for more than you currently owe on the property and paying off the old mortgage. Assuming you purchased the property significantly below market value and your credit is in pretty good shape, you may be able to turn right around after the purchase and refinance to cash out that equity.

I say "may" because some lenders won't refinance a mortgage until after you've owned a home for six months and a day or a year and a day. The reason for this is because a house is only worth what you actually paid for it or what it appraises for, whichever is lower. A home equity loan to cover repairs and renovations, however, is often easier to obtain.

TIP

You don't have to cash out all the equity in a property. You can cash out a portion of it to cover repairs and renovations and cash out the rest of the equity when you sell the property.

When refinancing to cash out the equity in a home, be as careful shopping for mortgages as you were when you borrowed the money to purchase the property. Avoid high-cost loans and any loans that have pre-payment penalties, especially if you're planning to place the house back on the market soon. See Chapter 5 for guidance on shopping for low-cost loans.

Reselling the Property to the Previous Owners . . . Or Their Family

After you officially own a property, it's yours to sell, and the previous homeowners have to move out . . . if they didn't move out already. Sometimes after foreclosure, however, the homeowners break the news to other family members who are in a position to bail them out by loaning or gifting them some money or buying the house and letting them live in it. In such cases, you may be able to sell the property back to the original owners or their family.

In the following sections, I reveal some do's and don'ts that apply to these situations along with some of the positive aspects of selling a foreclosure back to the previous owners.

Reselling to the previous owners

The previous owners are likely to do whatever it takes to remain in their home. If their financial situation has improved since the foreclosure or friends and family members have offered them a good chunk of cash, they may now be in a position to buy back the property. The opportunity, however, is not always available or attractive for you as an investor. Keep the following caveats in mind:

- If the property has any liens against it that were wiped off the books by the foreclosure, those liens reattach themselves to the property if the previous homeowners buy it back. This can often drive the homeowners back into foreclosure, which isn't something you or they really want.

- You can't strip the homeowners of all the equity they have built up in the property. Say, for example, you purchased a property worth $300,000 for $175,000. If you sell it back to the previous homeowners for $300,000, you've taken all the equity out of the house. You have two options here — sell the house to someone else for $300,000 or sell it back to the previous owners at a discount of say $225,000. Whatever you do, you don't want to be an equity stripper. See the following sidebar, "Equity stripping — Don't do it!" for details.

Equity stripping — Don't do it!

Homeowners who are facing foreclosure are often unaware of their options and of just how much equity they have built up in their property. They may have been making their monthly mortgage payments for 10 or 15 years while housing values in their neighborhood have been rising at a rate of 5 to 10 percent annually. They're completely unaware that the house they bought for $100,000 ten years ago is now worth $150,000, and they've paid off about $14,000 of the principal, so they now have $64,000 worth of equity. All they see are the monthly bills coming in that they can't pay.

The homeowners' ignorance of the amount of equity they have built up in their home can make them vulnerable to predatory lenders and other crooks who want to cash out that equity for themselves. These equity strippers employ a variety of schemes to bleed this money out of the homeowners, including schemes such as these:

- Mortgage brokers attempt to convince the homeowners to refinance their way out of a financial setback by taking out a loan with higher monthly mortgage payments than the homeowners can afford. The mortgage broker rakes in the payments until the homeowners run out of money, and then the lender forecloses on the property.
- Crooked investors convince homeowners who have a substantial amount of equity built up in their property to sell the property to them for significantly less than the property is worth. The "investor" may promise the homeowners that they can continue living in the home indefinitely, and then, as soon as the homeowners sign the papers, the con artist evicts them.
- Con artists offer to save the homeowners from foreclosure. All the homeowners have to do is sign a quit claim deed over to the con artist, and the con artist will take care of everything. What the con artist does take care of is re-conveying the property's title to his own name.
- A con artist may offer to buy the home from the homeowners and lease it back to them. The con artist collects the monthly rent and never pays off the underlying mortgage, so the homeowners lose their rent money and lose the house in foreclosure.

If you buy a property directly from homeowners facing foreclosure or at auction for a bargain-basement price and then sell the property back to the homeowners at full-market value, you're practicing yet another form of equity stripping, which the courts frown upon. Whether or not you get caught, it's still wrong, and if you do get caught, you can look forward to a hefty fine and perhaps some jail time or at least undoing the transaction and having to put the homeowners back in the position they were in before they met you.

Why would you agree to accept less than full-market value for the house? Whenever I can earn a quick, tidy profit on a house and do the right thing for the homeowners, I jump at the chance. Usually, I develop a close relationship with the homeowners during the foreclosure process, and I don't want to destroy their trust by taking them to the cleaners. In addition, I don't want to ruin my reputation in the community — I'm in it for the long-term. If I treat the homeowners fairly, they're likely to recommend me to others they know who find themselves in similar situations. If you can earn a fair profit while helping your fellow man and woman, I strongly encourage you to do so. Otherwise, simply have them move out and sell to someone who can afford to pay the full price.

Another reason you may want to consider selling the property back to the previous owners comes down to simple economics. Say you're facing the likelihood of holding the property for six months. At $100 per day in holding costs, you're looking at a total bill of $18,000. On top of that, figure closing costs of 7 percent on $200,000 (a total of $14,000), and your bill is now up to $32,000. Now figure in your time and effort plus the costs of repairs and renovations. Sure, the homeowners get a break, but you also save yourself some money.

Life-saving life insurance

I recently had a very positive experience with a man who lost his wife and had substantial life insurance policy proceeds coming to him. He had suffered with his wife's illness on and off for the last few years, struggling to keep things together both at home and at work.

I bought the house in foreclosure not knowing the situation beforehand. The man's wife was in fact still alive when the foreclosure happened. About a month or so before the end of the redemption period, she passed away. He was now being forced to deal with the foreclosure on top of it all.

He told me he would like to buy the house back and that he would do so with cash from the life insurance, but that the check wouldn't arrive until after the expiration of redemption. I spoke with him and his family quite extensively, and what he ultimately decided was to use the money to buy something else. I think he made the right decision. The house needed some work, and he didn't feel that he was up to the challenge.

He decided to buy a condo, pay cash, and let someone else worry about the upkeep. I worked with him and gave him plenty of time — first to mourn, and then to close on his new condo and move. He worked with me, and I with him, and he left the house nearly spotless.

Sometimes doing the right thing means you wait a little longer for your profits. I sold that house and made my money, he got a fresh start without the burden of the house, and I know that the time I waited will pay off tenfold with positive word of mouth. He and his family couldn't stop thanking me for what I had done.

If you took out a traditional loan to purchase the property, your mortgage probably has a due on sale clause, which means you cannot sell the property back to the previous homeowners without the lender's approval.

If selling the home back to the previous homeowners is not an option due to the possibility of having other liens reattach to the property, you may be able to sell to a family member who agrees to let the homeowners remain living in the house.

Financing the buyback through insurance policy proceeds and other means

Homeowners are often unaware of assets and other collateral they may have to secure financing, or they come into some quick money after the foreclosure is a done deal. In such cases, you may be able to assist the homeowners in obtaining the funds needed to buy back the property simply by making them aware of their options. Following are two options that may be available:

- **Life insurance policies:** If the home ended up in foreclosure because one of the homeowners passed away and the homeowner had a life insurance policy, cashing out that policy may provide sufficient funds for the surviving homeowner to repurchase the property. In some cases, a serious illness drives a couple into foreclosure, and then the spouse who was seriously ill passes away leaving behind a life insurance policy that can cover the purchase price. See the following sidebar, "Life-saving life insurance."
- **Retirement savings:** You can borrow against some retirement plans for the purchase of a house. If the homeowners have sufficient retirement savings, they may be able to borrow against it to buy the house back from you.

Leasing the Property to the Foreclosed-Upon Homeowners

Families are often reluctant to move out of their home because they have kids in school. They really need to sell the house and find more affordable accommodations, but they don't want to force their kids to change schools. In such cases, you may want to consider purchasing the property and then leasing it back to the family until the kids move out or the family has more time to plan.

WARNING!

Don't jump into a lease agreement with the previous homeowners before you've performed some serious number crunching. If the homeowners couldn't afford the monthly house payments, don't sign them up for a lease that has them paying monthly rent they can't afford. You'll simply end up with some deadbeat renters and set the family up for another failure. Before offering them the option to rent, make sure they've resolved the issues that sent them into foreclosure and that they can afford the rent.

If you decide to rent out the property to the previous homeowners, consult your real estate attorney and have her draw up a lease agreement. Keep in mind that not everyone is cut out to be a landlord. See Chapter 18 for details about leasing the property and for recommendations on additional resources that can assist you in properly managing a rental property.

Offering a Lease-Option Agreement

When a buyer really wants to purchase a property but is not currently in the financial position to do so (whether they're the previous owners or some other buyers), you may consider offering them a lease-option agreement, as discussed in Chapter 9. Perhaps the buyers need more time to secure financing or fix something on their credit report, or they're waiting for an insurance check or some other payment. With a lease option, the buyers agree to rent the property from you for a fixed period with the option to purchase the property at the end of that period.

Lease options are not always viable, but if the homeowners can come up with a down payment and provide some assurance that they will be receiving money or be able to qualify for financing in the specified time, a lease option enables you to establish some revenue flow while you're waiting to sell the property. I usually structure lease-option deals as follows:

- **Down payment:** Normally I require 5–10 percent down. You may want more money down when dealing with buyers who've just been through foreclosure. You credit them for the down payment by taking it off the purchase price, but a substantial down payment assures you that they're serious. If they can't afford it, they can't afford it — let them move on.
- **Rent:** I usually specify that rent is due on the first of the month and set the rent at about 1 percent of the purchase price or as close to that amount as is affordable. You don't want to be too flexible, but you don't want to break the bank either. I offer a bonus for paying on time and add the monthly payments to the down payment.
- **Terms and conditions:** The agreement should spell out the lease term and conditions. Your lease-option agreement should contain a forfeiture

clause stating that non-payment results in the forfeiture of the option and the down payment. The agreement should also contain a statement that the option is exercisable at any time, with no prepayment penalty or anything like that. What I tell them is if you win the lottery and want to pay it off tomorrow that's fine by me. I want them to succeed, and I want to realize my profit — the faster the better.

Repeating the same mistake

Whenever you're working with homeowners who have a less-than-stellar track record, be careful. People tend to follow the same patterns and repeat the same mistakes.

I once purchased a foreclosure property at auction for $245,000. The house was worth about $550,000. The couple who owned the property was fairly affluent, but the wife, who was in charge of making the monthly mortgage payments, wasn't much of a money manager. She failed to make the payments and failed to tell her husband about it. The property ended up on the auction block, and I bought it. I actually won the auction with an overbid of $50,000 — that is, I bid $50,000 more than what was owed on the mortgage. That $50,000 was placed in escrow. The couple was entitled to it.

I could have sold the property for $550,000 and walked away with nearly $300,000 in profit, but when I heard the husband tell the story, I figured I'd give the couple a break and sell it back to them for about $300,000 — about $50,000 more than I had paid for it. I knew they had access to the $50,000 in overbid money, so that was a pretty good down payment, and the husband earned a good income, so the couple certainly had the means to regain their financial footing and could afford the house. The husband was going to take over the job of paying the bills. My attorney happened to be in my office that day and sat in on the interview. He advised me to have the couple move and sell the house at full value. I went against his advice because of the husband.

I offered the couple a lease-option agreement that gave them 12 months to buy back the house. They paid me the $50,000 down payment, and I gave them back $10,000 to help them cover their monthly bills. They managed to make their monthly payments for about five months. Then, they stopped making payments. What happened? After about five months, the wife insisted on re-assuming the responsibility of paying the bills, and the husband let her. As soon as he stopped managing the finances, the payments stopped. He didn't realize what was happening until I called and told him that they had forfeited the lease option.

During those first five months, they easily could have sold the house themselves for $550,000, paid me the balance of $250,000, and walked away with over $200,000, but they chose to stiff me. I took possession of the property, and they lost everything — the $50,000 overbid, their house, and the opportunity to make $200,000 free and clear. I didn't feel any sympathy for them. I had given them a break, and they went back to their same old patterns that got them in trouble in the first place.

When you're working with distressed homeowners, be careful. People often develop expensive habits and destructive patterns that are tough to break.

Make sure the renters understand that they are renting with an option. If they don't exercise their option during the option period, they may forfeit it. If they don't pay rent, they may forfeit it. Make the terms clear. Follow up with them throughout the lease-option period, ask how their mortgage hunt is coming along, and refer them to mortgage lenders you may know.

Tip during the paper-signing stage, we use a Dictaphone and ask permission to have the transaction on tape from beginning to end. I tell my client that this is a protection for all of us to make sure that we all live up to our parts of the agreement. I make sure that we're thorough, that we allow them to ask questions, and we encourage them to seek legal counsel.

Assigning Your Position to a Junior Lien Holder

Say you buy the first mortgage. Do you have to take possession of the property to make a buck? Nope. You can sell your position to a junior lien holder and avoid the ugliness of eviction and the hassles of repairing and renovating the property. Here's how it works, assuming you're working in an area with a redemption period:

1. **You buy the first mortgage, either at auction or by negotiating a short sale with the lender.** You now have controlling interest . . . just make sure you pay any back property taxes.
2. **You wait out the redemption period.** If the property has other liens against it and they decide to foreclose, another investor may buy one of the junior liens at sheriff sale. If another investor buys a junior lien on the property, the clock on that redemption period just begins to start ticking, while you're already partially through the redemption period on your investment.
3. **You approach the holder of the junior lien and say something like, "Look, if you buy my interest, I'll sign over my position to you."** Make your offer worth it for the junior lien holder; otherwise, she may be better off redeeming your lien and waiting a little longer. If your offer makes sense and the junior lien holder knows what she's doing, she'll find the offer attractive, because she gains not only your first mortgage but also your position in the redemption period rather than having to start from scratch.

Leveraging your position

Knowing the lien holder positions, as discussed in Chapter 15, can often open your eyes to win-win situations with other parties who have a financial interest in the property.

I purchased a first mortgage on a property at auction. The house had a second mortgage on it — a lien on it by the local police department and our county prosecutor. The owner pleaded guilty to drug dealing and had to pay a fine of about $50,000, which was taken as a lien against the house. We were about a week shy of the expiration of the redemption period, and the county was going to redeem us, meaning we stood to get our money back, and that was about all.

I knew from experience that the county didn't want to pay me off and then take possession of the property and have to sell it, so I called the prosecutor in charge of drug seizures in Macomb County and explained the situation to her. I told her that if she would agree not to redeem our first mortgage, we would split our profits with the county 50/50. It took me less than an hour to work out an agreement. She came back with a counteroffer. She wanted a guaranteed minimum of $20,000, which was a smart move on her part. I agreed.

We ended up taking possession of the property and selling it for a $37,000 profit. The county received the first $20,000, and we received $17,000. We sold the house pretty quickly and got what we wanted out of it, and the county was able to acquire $20,000 without the hassle of dealing with the property.

Had we not struck a deal, we would have walked away with nothing.

The take-home message here is that you have to remain constantly vigilant throughout the process and be prepared to deal with the other lien holders. Remain flexible and constantly on the lookout for win-win opportunities . . . otherwise, you may just find yourself the big loser.

Part VI
The Part of Tens

The 5th Wave By Rich Tennant

"...and don't ignore those incarceration moments. I can't tell you how many referrals I've gotten in a holding tank."

In this part . . .

No *For Dummies* title would be complete without a Part of Tens. The chapters in this part show you how to avoid the ten most common beginning blunders and ten ways to help homeowners navigate the foreclosure process in a way that convinces the homeowners to work with you rather than some other investor and maximizes your opportunities for future leads.

Chapter 20

Ten Common Beginner Blunders

In This Chapter

- Avoiding the mistake of underestimating costs and overestimating profits
- Steering clear of overestimating a property's profit potential
- Stifling your desire to overbid on a property
- Suppressing the urge to skip research and make assumptions
- Avoiding the tendency to start renovations too soon

The difference between profiting in foreclosures and losing your shirt often hinges on your ability to avoid the most common mistakes. In this chapter, I point out the ten most common foreclosure investment blunders so you don't have to experience them first hand.

Having Insufficient Funds on Hand

Novice investors often underestimate costs and overestimate the future sales price of a property or they take on too many projects and find that they're quickly in over their heads with maxed-out credit. To avoid these common pitfalls, I offer four suggestions:

- **Play it safe.** Overestimate costs and underestimate profits. After doing your research and calculations, if you're not fairly certain that you can earn a profit of 20 percent or better on a property, don't buy it. Wait for the right opportunity.
- **Start small.** Making mistakes on a half-million dollar property generally cost more than making those same mistakes on a $100,000 property. Holding costs alone on a half-million dollar property can sink a small-time, novice investor. Start investing in more affordable properties and work your way up slowly — take the crawl-walk-run approach.

- **Start slowly.** Buy, renovate, and sell one foreclosure property at a time and do each one right from start to finish. In your enthusiasm to become a wealthy real estate investor, you may be tempted to buy several properties at your first auction. Don't succumb to such temptations.
- **Don't rush a purchase.** Don't think you're failing because it has been three months and you haven't bought anything. Keep working on finding a property until the right opportunity comes along. Profits in real estate can be high, but mistakes are almost always costly.

TIP

By starting with one property at a time, you reduce your exposure to risk while learning from your mistakes. If you buy five properties all at once, you're likely to make the same mistake on all five properties. Buy one, make your mistakes, learn from those mistakes, and then avoid making the same mistakes on your next property. After you've eliminated all of your mistakes (something I'm still working on accomplishing in my 30 years of investing), consider taking on more projects.

Overestimating a Property's Value

Housing values don't exactly have a glass ceiling. The values of comparable homes in the same neighborhood set the upper limit on what you can expect. If you're thinking that you can break through the ceiling by transforming a shack into a showpiece, think again. You ultimately over-improve the house and end up giving away thousands of dollars in renovations as a housewarming gift to the buyers.

REMEMBER

You make your profit when you *buy* a house. Make sure you buy at a price that enables you to earn at least 20 percent on your total investment, which includes the purchase price, holding costs (monthly loan payments, property taxes, insurance, and utilities for the duration of the project), the cost of repairs and renovations, and the cost of selling the property.

Underestimating Your Holding Costs

Investors often take a hit on holding costs — property taxes, insurance, interest payments, and utilities paid between the time they purchase the property and the time they sell it. Holding costs can be particularly burdensome when you purchase properties in an up market and the market suddenly tanks. Anticipate daily holding costs to exceed $100 per day (over $3,000 per month), and carefully calculate your holding costs well in advance of any project. Sure $100 per day in holding costs seems a little steep, but I've done the math. Trust me, you can expect to pay $100 or more per day in holding costs. See Chapter 11 for more about holding costs.

Don't forget to account for holding costs through the duration of the redemption period, and whenever you pay property taxes and insurance premiums during this period, be sure to file an affidavit at the recorder's office, so if someone redeems the property, you can be reimbursed for these expenses.

Overbidding in the Heat of Battle

In Chapter 11, I cover the topic of bidding at foreclosure auctions in detail and warn you to set a maximum bid price and stick to it, but I can't emphasize this point enough. Bidding at auction is a very emotional experience that often drives up the price in a hurry. If you're anything like me, you hate to lose a property to another investor and are likely to bid yourself right out of a profit.

To avoid the temptation to overbid, write down your maximum bid amount prior to auction and look at it before the bidding starts. Consider having someone who's less emotionally involved accompany you to the auction and prevent you from exceeding your maximum bid amount. When the bidding rises above your upper limit, drop out. You'll always have another opportunity.

Failing to Investigate the Title

The title is the single most important document attached to the property. It contains the names of the legal owners of the property along with the names of any lien holders and the claims against the property. If you don't look at the title before you bid or make an offer on the house, you're flying totally blind with a completely disabled instrument panel. When you fail to inspect the title, you leave yourself wide open to the following risks:

- Buying a property that someone else has already recently closed on. Con artists may sell the same home to several different buyers and let the buyers sort out who really owns it. Don't assume this won't happen to you — it happens more often than you may think.
- Buying a junior lien thinking that you're buying the senior lien. After the foreclosure process runs its course, your junior lien may be wiped out, leaving you with nothing.
- Buying the house from the owners when some other investor has already purchased the senior lien without your knowledge. When homeowners get desperate, they may try anything, even fraud. Even if you research the title on your own, when buying directly from homeowners, purchase title insurance and hire the title company to manage the closing.

Always research the title before bidding on or purchasing a property from the homeowners. You can order a title commitment from your title company. In Chapter 8, I show you how to properly research a property to avoid the common pitfall of buying a house not knowing what you're buying. If you do the research yourself, double- and triple-check your work before you bid.

Failing to Inspect the Property with Your Own Eyes

Just because a property looks like a great investment on paper doesn't mean it's a great investment property. My crew came very close to purchasing a gutted shell of a home at auction, but fortunately one of my colleagues prudently did a walk around inspection and noticed that the back of the house was gutted by fire. The front and sides looked great!

Before you purchase a property, the least you should do is drive to the location, look around the neighborhood, and do a walk-around inspection of the property taking several photos of every side. Knock on the font door and try to engage the homeowners in a conversation. While conversing, try to look past them into the house. You may be able to convince them to invite you in, but don't count on it. Stop short of hopping the fence, so you won't be charged with trespassing or find yourself staring down the barrel of a gun — it's happened to me.

Bidding on a Second Mortgage or Junior Lien

Shortly after some real estate investment guru comes to town and stages a "free" seminar on investing in foreclosures, my office receives a rash of calls from distressed investors who reportedly followed the guru's advice and stood to lose a lot of money. In most cases, the person failed to research the title and ended up purchasing one or more second mortgages or junior liens, which were likely to be wiped out by the foreclosure process. In one case, an intelligent professional purchased over $100,000 in worthless paper during a single auction!

You can make money purchasing second mortgages or junior liens, but you really have to know what you're doing and remain constantly aware of the liens that hold precedence over yours. In Chapter 19, I introduce you to the strategy of buying and profiting from junior liens. However, I always advise beginners to steer clear of junior liens until they've gained some experience buying senior liens.

Never buy a junior lien unless you intend to purchase the senior lien at auction or redeem the property from the senior lien holder. Otherwise, you stand to lose your entire investment.

Renovating a Property before You Own It

In your enthusiasm to score a quick profit from your investment property, you may be eager to get inside and start renovating the property during the redemption period. Many investors have made this mistake and have paid dearly for it.

In areas that have a redemption period, the homeowners have the right to pay off the lien, along with any penalties and interests, at any time during the redemption period . . . up to the final day. If you invest time, money, and effort into repairing and renovating the property, and the owners decide to redeem, you lose all the time, money, and effort you invested. You may even face legal claims against you.

Some jurisdictions allow acceleration of redemption periods if the house is abandoned, but follow the required steps and have an attorney draft the paperwork and advise you on how to move forward legally.

Trusting What the Homeowners Tell You

Homeowners who are facing foreclosure are often willing to say anything to convince you to let them remain living in their home or paying them as close to full market value as they can get. They'll tell you the house is in perfect condition, they have money coming in, their grandmother just died for the third time this month, or promise they'll "move out as soon as they find a place," whenever that is. I've even had a couple tell me that their baby had died. Their baby hadn't died. Confirm anything that sounds fishy.

I can't blame people facing foreclosure for bending the truth. If I were in the same situation, I may be tempted to float a few white lies, myself. As an investor, try to retain your compassion, but don't believe everything you hear. Offer a suitable concession, have the homeowners agree to it (in writing), and then hold them to it. In Chapter 16, I offer some suggestions for perks to consider offering to encourage the homeowners to move on.

The cleverest homeowners tell you that the house is in really bad shape and that you will spend tons of money trying to fix it up — why not let them stay for a "reasonable fee?" It may be that the house is in terrible shape, but if it's in bad shape now, they probably made it that way, and now that you own it, do you really trust the residents to not devalue your investment even more? Remain compassionate, but firm.

Getting Greedy

For some investors, earning a fair profit isn't good enough. They drum up lies and deceptions to prevent distressed homeowners from understanding their rights and fully grasping the options at their disposal. Con artists will even steal homes from uninformed homeowners by befriending them and convincing them to sign a quit claim deed relinquishing all their rights to a property without paying the owners a fair amount.

The minute that you see only $$$$, you're on the road to failure. Your name becomes mud, or at least dirty water, and you start losing out on deals. I have yet to meet someone who has lost in the long run by taking the high road, but I know of many who've lost in the very short run by associating with crooks or following unethical practices. Be fair, be honest, be brutally honest some times, negotiate hard, be firm, keep your ultimate goal in mind (profits), but never compromise yourself for a buck.

Chapter 21

Ten Ways to Maximize Future Leads by Acting with Integrity

In This Chapter

- Encouraging homeowners to get a handle on their finances
- Convincing the homeowners to seek assistance from family and friends
- Persuading homeowners to contact their lenders
- Hinting at the bankruptcy option
- Suggesting legal options homeowners can explore

Throughout the book, I discuss the need to be on the level with homeowners who are facing foreclosure. Acting with integrity distances you from the foreclosure predators who take undue advantage of distressed homeowners.

By remaining on the level, you can gain a competitive edge by building a reputation as the trustworthy go-to guy or gal for homeowners who are facing foreclosure. In other words, your integrity brings you more leads (which is the bread and butter and vegetables and meat of real estate investing).

In this chapter, I offer ten tips to use your integrity to maximize future leads — ten ways you can assist homeowners even if your assistance results in a missed opportunity to earn a profit.

Stopping the Bleeding: Providing Basic Financial Advice

Unless you're a certified public accountant or a financial advisor, you can't offer homeowners bona-fide financial advice. Many homeowners who are facing foreclosure, however, could benefit from such advice. They need to figure out a way to get a handle on their finances, perhaps consolidate their debt, and commit to an austerity program to avoid overspending. You may not be qualified to provide such advice, but you can highlight the possible benefits of a debt counselor or financial advisor:

- Consolidate debts, possibly reducing the total monthly payments.
- Set realistic budget goals and establish a detailed budget.
- Negotiate with lenders to restructure payments or accept short sales. (For more about negotiating short sales, refer to Chapter 15.)
- Obtain advice on refinancing or selling the property to "get out from under it."

TIP

Another way to network your way to future investment opportunities is to establish mutually beneficial relationships with debt counselors and financial advisors. Just be sure you're not creating mutually beneficial relationships that compromise the homeowners' rights.

Assisting Homeowners in Their Job Search

A long-time friend of mine worked in a job placement agency. On a number of occasions, I found myself dealing with homeowners who had few options, because they were out of work. I would tell the homeowners, "I have one more trick up my sleeve. I'll place a call and see if my friend at the job placement agency can help you. Let me try, and I'll get back with you." When I called my friend, he would ask me what field they were in before they were fired or laid off, and I would tell him. In almost every case, he was able to find the homeowners jobs.

If the homeowners need a job, and you know of any openings, give them a hand. You'll experience immediate gratification, and your good deed is likely to reward you somewhere down the line.

Suggesting That the Homeowner Seek Help from Family and Friends

When you're trying to acquire a foreclosure property, it may seem counterintuitive to recommend that the homeowners seek assistance from friends and family members, but this is exactly what you should be doing. I always ask the question "Do you not want your relative to know?" The answer is almost always "Yes, we're embarrassed." "Well," I say, "Do you think it will remain a secret or be any less embarrassing when the bailiff comes to put your stuff on the curb?" I know that sounds harsh, but it often makes them stop and really think about it. A number of times this has prompted the homeowners to call a relative and get the help they needed.

If the homeowners do ask for and receive sufficient assistance to enable them to dig themselves out of foreclosure, you lose an opportunity to acquire the property, but you gain a friend for life. Assuming everything works out, the homeowners will sing your praises and refer you to the people they know who find themselves in similar predicaments. And even if they don't, you'll sleep better at night knowing you did a good deed.

In many cases, a friend or relative can offer only limited assistance, and the homeowners still face the inevitability of selling their home. If you've been on the level with them, they're more likely to contact you rather than some other investor when they need to sell.

Encouraging the Homeowners to Contact Their Lenders . . . and Soon

When homeowners fall behind on their mortgage payments, they're likely to go into hiding, avoiding bill collectors, attorneys, and anyone else who's looking for a payment. They're taking it one day at a time, hoping to hold on to their home for as long as possible.

Although this approach is perfectly understandable, denial and avoidance are the worst actions (or, more appropriately, inactions) homeowners can take. Inaction almost always leads to the loss of the home and any equity in it. Encourage homeowners to contact their lenders and other creditors immediately, describe their situation, and explore their options. If the homeowners refuse to contact their lenders, at least you know that option is off the table, and you can move on to the next option.

You may be able to act as the mediator between the homeowners and their lenders, but you'll need signed permission to do so. For details and a sample release you can request that the homeowners sign, refer to Chapter 9. Don't cross the line of giving advice that you're not qualified to offer. Tell the homeowners and repeat it often that you're not an attorney or an accountant.

Suggesting Short Sales and Other Debt Negotiations

Anxiety over debt, particularly large mortgage loans, can be so overwhelming to people that they lose perspective. Sure "it's only money" to people who have enough money to pay their bills and to a few slackers out there who don't worry about paying their bills, but to responsible homeowners who can't afford their monthly mortgage payments, the problem appears insurmountable. Many people don't even realize that lenders and other creditors will often agree to accept less than full payment on a debt.

Inform the homeowners that creditors often negotiate with people who owe them money. Describe the situation that the lender is facing — if the lender forecloses on the property, they may receive no payment whatsoever and end up having to pay the costs of repairing, renovating, and selling the property. The lender is often highly motivated to work with homeowners in these situations.

REMEMBER

A short sale is not always an attractive option for the lender. Also, you have to talk to someone who can make the decision. Most people handling the account for the lender are hourly employees who don't have the decision-making power. If the homeowners decide to explore this option, encourage them to start early — once the bank has decided on a plan of action, getting them to change course is like trying to stop a fully loaded freighter traveling at top speed.

Assisting Homeowners in Assessing Their Refinance Options

Distressed homeowners often overlook the power of the equity they've built up in their properties over the years. They experience a temporary financial setback, fall behind on their property tax payments to the tune of a few thousand dollars, and relinquish themselves to losing their home in foreclosure even though they have tens of thousands of dollars in equity built up in it.

Sit down with the homeowners, as explained in Chapter 9, and calculate the amount of equity they have built up in the home. They may be able to refinance their loan, consolidate their debts, and establish affordable monthly payments that get them out of trouble.

Refinancing out of foreclosure is not always an option. If the homeowners have bad credit, no foreseeable increase in income, and cannot refinance with a loan that provides them with affordable monthly payments, refinancing may simply put them back on track to facing a future foreclosure situation.

Suggesting the Option of Selling the House before Foreclosure

One of the best decisions many distressed homeowners can make is to scale back — sell their home and buy a more affordable home with lower property taxes, lower utility bills, and less maintenance. By selling the home, they can often pull out most, if not all of the equity they have in it, salvage their credit, and have a chunk of money to use as a down payment on their next home.

Of course, this option isn't open to everyone. If foreclosure is only a couple weeks around the corner, and the home is located in an area that has no redemption period, the homeowners aren't likely to have sufficient time to market and sell their home. If the homeowners have plenty of equity in the home and several months to act, then this option is usually the best option.

I'm a real estate agent, so I can list and sell a home and profit from the transaction even if the owners choose not to sell it to me. You may not be in the same position, but you should always present the homeowners with all of their options and let them decide what's best. If you're a real estate agent, you need to make sure you disclose this to the homeowner many times, by card and verbally, even if you represent yourself.

Bringing Up the Bankruptcy Option

I'm not a big fan of filing for bankruptcy, because it's usually a lose-lose situation for all involved. Even if the homeowners qualify for bankruptcy, it rarely erases their credit card debt and simply delays an inevitable foreclosure. Creditors can simply wait until the bankruptcy stay is lifted and then proceed with foreclosure.

As a foreclosure investor, however, you should always present bankruptcy as an option and inform the homeowners that they have a right to seek professional advice from an attorney. Attempting to discourage a homeowner from seeking legal counsel is illegal, not to mention just plain wrong. Don't even try to explain bankruptcy to them, and provide them with the names of several qualified attorneys, just in case one doesn't work out and the homeowners attempt to pin the blame on you.

Offering a Helping Hand

When you're working with distressed homeowners, think of creative solutions to assist homeowners in digging themselves out of their financial hole. I once met a homeowner facing foreclosure who was a hard worker — the kind of guy who always has a little grease under his fingernails, the guy you want working for you. I referred him to my friend at the job placement office, and my friend called me later that afternoon. He said, "You know that guy you sent me?" And I said, "Yeah, what about him?" My friend replied, "He showed up here in stained overalls and a beat-up ball cap with grease under his fingernails. His resume was on a folded up piece of lined loose leaf paper with the names and phone numbers of where he worked and descriptions of what he did at all those places . . . all hand-written, of course."

"No, I didn't know that, but it doesn't surprise me," I said.

"Wait a minute," my friend said, "You sent me over the roughest looking guy who has ever walked into my office, and you know what . . . he's absolutely perfect! I had an employer who just gave me an opening for some sort of specialty hydraulic work, and this guy has ten-plus years of experience in that very field. I called the references on that tattered resume, and each and every one said the same thing — 'If we I could have kept him on I would have, he'll be your top worker — not many like him.'" My friend then went on to say that the guy was starting his new job the next day.

Later, I received a call from the homeowner, and he couldn't thank me enough. He was sorry that I wasn't going to make any money, because now he wouldn't need my help saving his house, but he was so very thankful. He said "You just got me a new lease on life. Things are going to be okay." And they were.

I didn't make money on the deal, but my name was gold to that man, and when his mother passed away and he wanted to sell her house for cash, who do you think he called? Well, he didn't actually call, he came in and saw me. He said he wouldn't think of working with anyone else. Win-win? I think if you look up the definition, this story is right there.

Revealing the Option to Walk Away

Few lenders will pursue homeowners who simply vacate the premises, but I would never personally recommend that someone just head out of town when facing foreclosure. Walking away without a trace usually leaves a trace on the homeowners' credit history, which makes obtaining future loans much more difficult.

A better way to walk away from a property is to either sell it to an investor who can then deal with the lenders, or offer the lenders a deed in lieu of foreclosure with the agreement that the foreclosure will not show up on the homeowner's credit history, and that the homeowner won't be responsible for any deficiency that might arise after the sale of the house. (Some states allow for deficiency judgments, in which the lender can pursue the homeowner after the sale for a portion or all of the money the lender lost when the homeowner defaulted on the loan.) I discuss this option in greater detail in Chapter 2. Deed in lieu of foreclosure is usually an attractive option only for homeowners who have negative equity in the property and no investor willing to pay them to move on.

TIP

If the homeowners have no or negative equity in their property, crunch the numbers and see if you can come up with an offer that's better than the deed in lieu of foreclosure option. The homeowners can still walk away from the property, but they walk away with some cash in their pockets, and you end up with the property — after paying off the senior lien holder, of course.

Chapter 22

Ten Tips for Avoiding Common Foreclosure Minefields

In This Chapter

- Turning up your nose at get-rich-quick schemes
- Verifying facts and figures with vigilant research
- Investing with your head, not your heart
- Creating win-win transactions by dealing above board
- Coping with guilt and blame

If foreclosures were risk-free, easy money, everyone with a little cash and motivation would be buying and selling foreclosures. However, the risks are very high, and one minor misstep can tip the balance from glowing success to financial failure.

In this chapter, I point out the most serious and common problem areas in an attempt to steer you clear of buried mines, including get-rich-quick schemes, misleading information, the natural impulse to let emotions drive decisions, the common temptation to take advantage of distressed homeowners, and the disappointment and guilt that often paralyzes even the most empathetic foreclosure investor.

Steering Clear of Foreclosure Investment Scams

Every segment of the real estate market seems to attract con artists. Most of these fraudsters are quite intelligent and more than capable to make an honest living in real estate. In fact, a wide majority of them would make more money putting their energy, knowledge, and experience into more productive and honest pursuits. Instead, they prefer to exploit vulnerabilities in the system and to prey on distressed homeowners.

When you're first starting out in foreclosure investing, you, too, may be vulnerable to the silver-tongued promises of the slick, fast-talking con artist who promises quick, easy profits. To spot the signs of a typical real estate investment con artist, check out John T. Reed's Real Estate Detection B.S. List at `www.johntreed.com/BSchecklist.html`.

Researching the Title Yourself

Buying any property, first and foremost, is a legal transaction. To ensure that everyone involved in the transaction, including the seller, buyer, and lender, are protected and that the transfer of property from one owner to the next is legal, county offices record several documents that are publicly accessible, including the deed, title, mortgage (and note), and city records.

Before buying a house, have your title company supply you with a title commitment and examine it carefully, so you know what you're getting yourself into. See Chapter 8 for details on researching the paperwork.

Inspecting the Property with Your Own Eyes

You wouldn't buy a used car without test-driving it, kicking the wheels, and taking a peek under the hood. Yet, many novice foreclosure investors do just that. They walk into a foreclosure auction, plop down tens of thousands of dollars for a property they've never even glanced at, often without knowing where it's located. They would probably have a better chance of making a profit by buying lottery tickets.

As a real estate investor, "my eyes or no buys" should be your credo. Until you see a property with your own eyes, you don't know what it is, what kind of condition it's in, or the condition of the properties on the same block.

Knowing What You're Bidding On

Novice investors often purchase "properties" at foreclosure completely unaware that they just bought a second mortgage for $30,000 that's almost guaranteed to be wiped off the books once the first mortgage is foreclosed on. They buy what almost assuredly will become a worthless piece of paper.

When you decide to buy a foreclosure property at an auction, realize that you may be bidding on any of the following:

- Senior liens (first mortgages)
- Junior liens (second mortgages or other claims against the property)
- Tax liens (for unpaid property taxes)

REMEMBER

Prior to an auction, carefully research the title, so you're aware of all lenders and other parties that have a claim against the property. That way, you know whether the lien being auctioned is a senior, junior, or tax lien, and you can bid accordingly. When you're first starting out, bid only on senior liens or tax liens.

Setting Realistic Goals

I don't want to be a wet blanket choking out the fire of your enthusiasm, but I do want to encourage you to start slowly. Set a realistic goal of buying one or two foreclosure properties in your first year. Next year, you may want to buy one every quarter. The following year, you may be prepared to buy a property once a month or even more frequently if you have a strong support team and the necessary financial foundation in place.

TIP

Do your first foreclosure right — focus on one property from start to finish. See how it goes, log your mistakes, and then, when you're ready for your next property, repeat the process — without the mistakes this time. If a transaction flops, don't give up. The knowledge you gain in a failed attempt can only improve your chances of future success.

Muffling Your Emotions

When you're dealing directly with distressed homeowners, empathy is the most effective and appropriate response. As a real estate investor, however, this is business, so avoid becoming too emotionally involved in the process. The following list provides specific emotional guidelines to follow:

- **Avoid emotional connections with distressed homeowners.** Desperate homeowners often take desperate measures to remain in the home, trying to play your emotions against your business sense. You've arrived to help them out of the hole they're in, not to have them drag you into the same hole.

- **Leave your emotions at home when you attend an auction.** If your love for a property or your obsession to outbid the competition leads you to pay more for a property than it's worth, you lose.
- **Funnel frustration into determination, not anger.** You need others to assist you in gathering the information you need and performing the work required to turn a profit. Anger only turns the people you need against you. Every problem has a solution. Solve the problem rather than blaming others.
- **Don't despair.** It is so totally not cool.

Investing with Integrity

Some con artists who call themselves real estate investors seem to believe that anything they can do to get their grubby little hands on a house is good business. They justify their immoral and often criminal actions by saying things like:

> "Everybody's doing it."
>
> "I didn't twist anybody's arm. They could have said 'No.'"
>
> "If they had paid their mortgage and taxes, they never would have had to deal with me."

Admittedly, these statements are all true, but certain actions cross the line that divides good and bad, ethical and unethical, legal and illegal. Here are some practices that clearly cross the line:

- Withholding information from the homeowners that could enable them to sell the house themselves and extract some equity from the property.
- Misleading homeowners into believing that the only option they have is to sell the property to you.
- Befriending the homeowners to convince them to sell the property to you, even when that's not in their best interest.
- Buying the tax lien and then convincing the homeowners to move out because you now own the property, even though they could pay the back taxes and retain possession of the home.
- In a state that has a redemption period, buying the property at auction and then informing the homeowners that you bought the property and they need to move out immediately without informing them of their redemption rights and the amount of time they have to redeem the property.

- Cheating the homeowner out of *overbid* money. An overbid occurs when an investor pays more for the property at auction than what is owed on the property. The overbid amount is used to pay off junior lien holders first, and then any remaining money belongs to the homeowners. Con artists often try to charge the homeowners, sometimes 50 percent to help them claim the overbid money. Other con artists simply take it all.

If you feel that what you're saying to homeowners is not in their best interests, then you're probably doing something wrong. Of course, you want to make a profit, so what's in your best interest counts, too, but not to the point of misrepresenting the facts.

Anticipating Delays

Many of the most experienced and successful real estate investors refuse to deal with foreclosures, because foreclosures can be so messy and drawn out. In a way, that's good for you — less competition from the high rollers — but you have to prepare yourself for the messiness.

Because the successful foreclosure buyer must be patient, you have to calculate delays into your formula. Realize that any of the following delays often result in your having to wait before you realize your profit:

- Homeowners taking their sweet time to make a decision
- Courts or trustees taking their sweet time to resolve the issue
- Homeowners changing their minds at the last minute
- Redemption periods that can last from several months to a year

Don't count on quick-cash deals when you're investing in foreclosures. If you're investing part time, keep your day job. You need steady income, so you can afford to be patient. If you need the profit from a foreclosure property to pay the bills, the stress of waiting may be enough to convince you that investing in foreclosures isn't exactly the best option for you.

Foreseeing Unforeseen Expenses

Investing in real estate is not rocket science. You can't calculate to the penny how much a property is going to cost, because of all the variables involved. Although you can't completely prevent unforeseen expenses from sinking your budget, you can reduce the risk by creating a buffer and at least considering the following expenses:

- Purchase price is something you control, so set the price with the goal of making a 20 percent or better profit.
- Repair and renovation expenses.
- Holding costs include stuff like property taxes, interest on loans, insurance, and utilities for the duration of the project — the redemption period (if applicable in your area), time to repair and renovate the property, and time to sell it.
- Real estate commissions, if you hire an agent to sell the property.
- Transfer tax is sort of like sales tax, which varies from one locale to another.
- Research fees for the title work and any other documents you need.
- Recording fees, particularly at closing.
- Miscellaneous expenses, including mileage and phone calls.

TIP

Underestimate your profit, overestimate your expenses. See Chapter 10 for guidelines on how much you can afford to pay for a property to be fairly certain of a profitable investment.

Dealing with the Blame and Guilt

In some people's eyes, foreclosure investors are the scum of the earth, stealing homes from poor, unfortunate homeowners and old ladies. As a foreclosure investor, you'd better be able to deal with the contempt you're about to face. Many real estate investors simply can't handle it, and they look for the exits after investing in only one or two properties.

To steel yourself from the disdain you're likely to face, keep in mind that you didn't cause the predicament the current homeowners are in. They're in this predicament either due to their own foibles or some unforeseen, financially stressful event that's outside their control. You've arrived on the accident scene with a possible solution to their current problem.

Appendix

Foreclosure Rules and Regulations for the 50 States

When you're playing the foreclosure investing game, you need to play by the rules. Here I provide you with the rules and regulations governing foreclosure in each of the 50 United States as well as the District of Columbia, and I offer some additional research resources where you can obtain more detailed information.

TIP

For each state, we provided contact information for the Realtor in the state who contributed the foreclosure information. To locate other qualified Realtors, visit `www.realtor.com`, where you can search for a Realtor by city and state.

To decipher this information, keep the following definitions in mind:

- **Deed type:** Deed of trust, mortgage deed, or both. A *deed of trust* is a mortgage contract that places control of the deed in the hands of a third party — a trustee. The trustee has the power to foreclose on the property in the event that the borrower defaults on the loan. A *mortgage deed* is a contract between the lender and borrower that gives the lender the right to foreclose on the property in the event that the borrower defaults on the loan.
- **Foreclosure process:** Judicial, nonjudicial, or both. A *judicial* foreclosure process is followed when no power of sale is provided in the mortgage or deed of trust; lenders must file a lawsuit to obtain a court order to foreclose on a property. A *nonjudicial* foreclosure process occurs when a power-of-sale is pre-authorized in the mortgage or deed of trust, in which case, the lender is given the right to foreclose on the property and sell it to pay off the balance of the loan in the event that the borrower defaults on the loan.
- **Process period:** This is the average amount of time that the foreclosure process takes from the time a foreclosure notice or notice of default is presented until the time that possession is transferred to the new owner.

- **Notice of default:** A notice that some states require be sent to homeowners notifying them that they have failed to fulfill their payment obligations as borrowers. Here, I specify whether a notice of default is required by the state.
- **Notice of sale:** An official announcement that specifies the time, place, and terms of a foreclosure sale and typically includes a description of the property, the names of the mortgagor and mortgagee, and other information. In most states such a notice must be published and posted in a public location and sometimes at the property for several weeks prior to the sale.
- **Redemption period:** Most states have a mandatory redemption period after the sale, during which time the foreclosed upon homeowners have a right to redeem their property by paying off the loan along with any interest and penalties. Here, I specify whether the state has a mandatory redemption period, and if it does, the length of that redemption period.

The information provided here offers a general overview of the rules and regulations governing foreclosure in each state. These rules and regulations may vary from one county to another, so consult your real estate attorney and the county clerk or register of deeds for additional details and clarification.

Alabama

Contributor: Sandra Nickel, (800) HAT-LADY, Sandra@HatTeam.com, www.InvestInMontgomeryAlabama.com

Contributor: Mike Keracher, (256) 549-1433 ext 101, Mike.Keracher@RealtyBid.com, www.RealtyBid.com

Deed type: Deed of trust and mortgage deed

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 60–90 days

Notice of default: Not required by state, but may be required by mortgage

Notice of sale: 3 weeks in a local newspaper and posted at the courthouse and 3 other public places, or as specified in mortgage

Redemption period: Yes, 12 months

Alaska

Contributor: Kristan Cole, (907) 373-3575, Kristan@KristanCole.com, www.KristanCole.com

Deed type: Deed of trust and mortgage deed

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 90 days

Notice of default: Varies

Notice of sale: 4 consecutive weeks in local newspaper and also in 3 public places, including the closest U.S. Post Office, 30 days prior to the sale date

Redemption period: 12 months, judicial; none, nonjudicial

Arizona

Contributor: Mario Romero, (602) 252-4191, Mario@MarioRomero.com, `www.TheRomeroTeam.com` or `www.MarioRomero.com`

Deed type: Deed of trust

Foreclosure process: Nonjudicial

Process period: 90

Notice of default: None required

Notice of sale: 4 consecutive weeks in local newspaper, with the last notice appearing no fewer than 10 days prior to the sale; mailed to the borrower and all other lien holders at least 3 months prior to the sale; posted on the property and at the courthouse at least 20 days prior to the sale

Redemption period: None

Arkansas

Contributor: Roddy McCaskill, Sr., (501) 312-2300, roddy@mccaskillrealty.com, `roddymcaskill.com`

Deed type: Deed of trust and mortgage deed

Foreclosure process: Judicial and nonjudicial

Process period: 90–120 days

Notice of default: Required to be filed with county (nonjudicial only) and mailed to the borrower

Notice of sale: 4 consecutive weeks in local newspaper, with the final notice appearing at least 10 days prior to the sale, and posted in the office of the county recorder

Redemption period: 12 months, judicial; none, nonjudicial

California

Contributor: Brandon Fairbanks, (559) 683-7268, bfairbanks@sti.net, www.mymaderacountyrealestate.com

Contributor: Tom MacDonald, (209) 342-2465, tmacdonald@pmz.com, TheMacDonaldGroup.com

Contributor: Terry Moerler, (805) 777-7777, Terry@TheMoerlerTeam.com, www.TerryMoerler.com

Deed type: Deed of trust and mortgage deed

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 120 days

Notice of default: Required to be filed with county and mailed to the borrower and other parties who have a claim against the property

Notice of sale: 3 consecutive weeks in local newspaper, starting at least 20 days prior to sale; recorded with the county at least 14 days prior to sale; and posted on the property and in one public location at least 20 days prior to sale

Redemption period: 365 days, judicial; none, nonjudicial

Colorado

Contributor: Kristal Kraft, ABR, CIPS, CRS, (800) 319-7738, Kristal@KristalSellsDenver.com, www.kristalsellsdenver.com

Contributor: Jo Ellen Nash, 800-SEL-VAIL (735-8245), jnash@joellennash.com, www.nashvail.com, www.vailforeclosure.com

Deed type: Deed of trust

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 45–180 days

Notice of default: None required

Notice of sale: 5 weeks in local newspaper and mailed to the borrower

Redemption period: 75 days (residential property), 180 days (agricultural property)

Connecticut

Contributor: Chip Neumann, (203) 438-0455 or (800) 966-0455, chip@neumannrealestate.com, www.chipneumann.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 60–150 days

Notice of default: None required

Notice of sale: Attorney assigned to sale publishes sales notice

Redemption period: Court decides

Delaware

Contributor: Tom Kashner, ABR, (302) 346-0569, tomkashner@exitsellshomes.com, www.tomsellsdelawarehomes.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 210–300 days

Notice of default: None required

Notice of sale: 14 days, posted in public places, on the property, in two local newspapers (no more than 3 times per week for 2 weeks prior to sale), and delivered to borrower (at least 10 days prior to the sale)

Redemption period: None, although the borrower can contest the sale prior to the court's confirmation of sale

District of Columbia

Contributor: D'Ann Faught, (571) 244-1827, jdfaught@gmail.com, www.searchdcmetrohomes.com

Deed type: Deed of trust and mortgage deed

Foreclosure process: Nonjudicial and judicial (rarely)

Process period: 30–60 days

Notice of default: Required to be sent to borrower

Notice of sale: Required, must be mailed 30-days prior to the sale date to the homeowners by certified mail, recorded with the county, mailed to the mayor or mayor's agent, and sent to any other lien holders. Notice of sale must also be posted as specified in the mortgage deed or deed of trust or advertised in the local newspaper at least 5 weeks leading up to the sale.

Redemption period: None

Florida

Contributor: Christine Adler, (954) 785-2900, Christine@AdlerTeam.com, www.AdlerTeam.com

Contributor: Gail Bass, (561) 981-3506, Gail@BassGroup.com, www.BassGroup.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 150–180 days

Notice of default: Not required by state, but may be required by mortgage

Notice of sale: 2 consecutive weeks prior to the sale, in a local paper or legal news publication, with the second notice published at least 5 days prior to sale

Redemption period: None

Georgia

Contributor: Leslie Edwards, (770) 460-9448, Leslie@LeslieEdwards.com, www.LeslieEdwards.com

Contributor: Donna Rennie, (404) 694-6408 or (770) 217-0088, Donna@DonnaRennie.com, www.DonnaRennie.com

Deed type: Deed of trust and mortgage deed

Foreclosure process: Nonjudicial and judicial (rarely)

Process period: 60–90 days

Notice of default: Not required by state, but may be required by mortgage

Notice of sale: 4 consecutive weeks prior to the sale in a local news or legal publication, and sent to borrower at least 15 days prior to the sale

Redemption period: None

Hawaii

Contributor: Carol M Paris, (808) 224-7071, carolparis@hawaii.rr.com or carol@carolparis.com, www.HomesInHawaii.com

Deed type: Deed of trust and mortgage deed

Foreclosure process: Nonjudicial and judicial

Process period: 180 days (nonjudicial), 330 days (judicial)

Notice of default: Required by the sale clause in most mortgages

Notice of sale: 3 consecutive weeks prior to the sale in a local newspaper, with the last notice appearing at least 14 days prior to sale; and sent to borrower at least 21 days prior to the sale

Redemption period: None

Idaho

Contributor: Sid Lezamiz, (208) 734-7007, Sid@LezamizRealEstate.com, `www.lezamizrealestate.com`

Deed type: Deed of trust and mortgage deed

Foreclosure process: Nonjudicial and judicial (rarely)

Process period: 150–180 days (nonjudicial), 330 days (judicial)

Notice of default: Mailed to borrower and anyone who has requested notification and filed with the county recorder

Notice of sale: 4 consecutive weeks, with the final notice appearing at least 30 days prior to sale; 120 days prior to sale, notice of sale must be mailed to the borrower

Redemption period: 365 days, judicial; none, nonjudicial

Illinois

Contributor: Sharon Falco, (630) 307-2060, Sharon@Sharonfalco.com, `www.sharonfalco.com`

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 300–360 days

Notice of default: None required

Notice of sale: 3 consecutive weeks prior to sale in the legal notice and real estate sections of a local newspaper, with the first notice appearing no more than 45 days prior to sale, and the last notice appearing no less than 7 days prior to sale; notice must be sent to the borrower and others who have a legal claim to the property

Redemption period: 90 days

Indiana

Contributor: Cathy C. Russell, (765) 426-7000, cathy@russellteam.com, CathyRussell.com

Contributor: Connie Kelley, (317) 513-8498

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 150–270 days

Notice of default: None required, but most lenders do deliver a notice of default to the borrowers

Notice of sale: 3 consecutive weeks prior to sale in a local newspaper, with the first notice appearing at least 30 days prior to sale; and in at least 3 public places, in the county courthouse, and delivered to the borrower by the sheriff

Redemption period: None

Iowa

Contributor: Dick Mathes, (641) 423-HOME (4663) or (877) 421-HOME (4663), DickMathes@DickMathes.com, www.RelocationIowa.com

Deed type: Mortgage deed

Foreclosure process: Judicial and nonjudicial (by request)

Process period: 120–180 days

Notice of default: Required

Notice of sale: 2 weeks prior to sale in a local newspaper, with the first notice appearing at least 4 weeks prior to sale; and in at least 3 public places, including the county courthouse, and delivered to the borrower (if still residing in the property) at least 20 days prior to the sale

Redemption period: Varies

Kansas

Contributor: Char MacCallum, (913) 782-8857, Char@Char4Homes.com, www.Char4Homes.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 12–24 months

Notice of default: Required

Notice of sale: 3 consecutive weeks prior to sale in a local newspaper

Redemption period: 3 months if owner vacates the house or 6 months if owner remains

Kentucky

Contributor: Mike Parker, (859) 647-0700, Mike@MikeParker.com, `www.MikeParker.com`

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 180 days

Notice of default: None required

Notice of sale: 3 consecutive weeks prior to sale in a local newspaper

Redemption period: 12 months

Louisiana

Contributor: Linda Gaspard, (225) 298-6889, homes@lindagaspard.com, `www.lindagaspard.com`

Deed type: Mortgage

Foreclosure process: Judicial

Process period: 180–270 days, typically 60 days

Notice of default: None required, but mortgage may require it

Notice of sale: 2 times prior to sale in a local newspaper (in the parish where the property is located); and personally served to the homeowner by the sheriff; must be advertised for a minimum of 30 days

Redemption period: None, deficiency judgments are allowed

Maine

Contributor: Ann Cummings, (603) 431-1111 ext. 3839 or toll-free (888) 349-5678 ext. 3839, ann@anncummings.com, `www.AnnCummings.com`

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 180–210 days

Notice of default: Required to be delivered to homeowner prior to foreclosure

Notice of sale: 3 weeks prior to sale in a local newspaper

Redemption period: 90 days

Maryland

Contributor: Rachel A. DeHanas, (301) 870-1717, Rachel@dehanas.com, www.dehanas.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial

Process period: 60–90 days, but usually takes longer

Notice of default: Not required but usually provided

Notice of sale: 3 consecutive weeks prior to sale in a local newspaper; and notice must be sent to the borrower and any other lien holders at least 10 days prior to the sale

Redemption period: Court decides

Massachusetts

Contributor: Jay McHugh, (617) 566-0300 ext. 202, JayMclb@aol.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial

Process period: 75–90 days

Notice of default: Not required by state but may be stipulated in the mortgage

Notice of sale: 3 consecutive weeks prior to sale in a local newspaper, with the first notice appearing no less than 21 days prior to sale; and notice must be sent to the borrower and any other lien holders at least 14 days prior to the sale

Redemption period: None, but the borrower is entitled to any overbid proceeds (money paid at the sale in excess of what the borrower owed)

Michigan

Contributor: Ralph Roberts, (586) 751-0000, RalphRoberts@RalphRoberts.com, www.RalphRoberts.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial

Process period: 90–420 days

Notice of default: Not required by state but often stipulated in the mortgage

Notice of sale: 4 consecutive weeks prior to sale in a local newspaper or legal publication, with the first notice appearing no less than 28 days prior to sale; and notice must be posted on the property for the same period during which the publication appears

Redemption period: 6–12 months, none if vacant

Minnesota

Contributor: Jeff Scislow, (952) 431-3900, Jeff@scislow.com, www.scislow.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 120 days, not including redemption

Notice of default: Required

Notice of sale: 6 weeks prior to sale in a local newspaper or legal publication; and notice must be given in person to the borrower at least 4 weeks prior to sale

Redemption period: 6–12 months

Mississippi

Contributor: Chester Harvey, (228) 875-8700, chester@chesterharvey.com, www.chesterharvey.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 90–120 days

Notice of default: Required 30 days prior to sale

Notice of sale: 3 weeks prior to sale in a local newspaper; and notice must be posted at the county courthouse

Redemption period: None

Missouri

Contributor: Janet Parsons, (417) 841-1111, Janet@JanetParsons.com, www.janetparsons.com

Contributor: Michael J. Maher, (816) 84-CONDO, Michael@TheMaherTeam.com, www.KansasCityHomeTeam.com

Deed type: Mortgage deed and deed of trust (more common)

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 21–45 days

Notice of default: Required

Notice of sale: Three weeks prior to sale in a local newspaper (where the property is located); in counties that have a city with more than 50,000 residents, the notice must be published for 20 days prior to sale with the last notice appearing on the day of the sale; in other counties, the notice must be published once a week for 4 weeks, with the final notice appearing no more than one week prior to sale; notice must be sent to the borrower and other lien holders at least 20 days prior to sale

Redemption period: Only applicable if the buyer at action is the lender, and the borrower expresses the intent to redeem at least 10 days prior to sale. The borrower must then post bond within 20 days after the sale in an amount that covers the mortgage interest, secondary loan interest, expenses, damages, and 6 percent interest. Assuming the borrower can meet these conditions, the borrower has 12 months from the time of sale to redeem.

Montana

Contributor: Cheryl Frei, (406) 598-8037, cherylfrei1@bresnan.net, cherylfrei.point2agent.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial

Process period: 150–180 days

Notice of default: Not required, unless required by mortgage

Notice of sale: 3 consecutive weeks prior to sale in a local newspaper; mailed to the borrower at least 120 days prior to sale; and posted on the property at least 20 days prior to sale

Redemption period: None

Nebraska

Contributor: Rosemary Horner, (800) 793-2550, Rosemary.Horner@woodsbros.com, `www.WoodsBros.com`

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 120–180 days

Notice of default: Required

Notice of sale: 5 weeks prior to sale in a local newspaper, with the final notice appearing 10–30 days prior to sale (for out-of-court foreclosure); 4 weeks prior to sale in a local newspaper (for court foreclosure)

Redemption period: None

Nevada

Contributor: Rosie and Curt Harsh, (702) 933-4500, Harsch99@aol.com, `www.finelasvegashomes.com`

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Contributor: Erick Harpole, CCIM, CRS, (775) 826-7653 or (800) 805-3755, Erick@HarpoleHomes.com, `www.HarpoleHomes.com`

Deed type: Mortgage deed and deed of trust (more common)

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 120–180 days

Notice of default: Required

Notice of sale: 3 weeks prior to sale in a local newspaper; in 3 public places at least 21 days prior to sale; and mailed to the borrower and any other lien holders

Redemption period: None, for out-of-court foreclosure; 12 months for court foreclosure, which is rare

New Hampshire

Contributor: Ann Cummings, (603) 431-1111 ext. 3839 or toll-free (888) 349-5678 ext. 3839, ann@anncummings.com, www.AnnCummings.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Nonjudicial

Process period: 90 days

Notice of default: Required by most mortgages giving the borrower 30 days to pay

Notice of sale: 3 weeks prior to sale in a local newspaper, with the first notice appearing at least 21 days prior to sale; and delivered to the borrower at least 26 days prior to sale

Redemption period: None, for out-of-court foreclosure; 12 months for court foreclosure, which is rare

New Jersey

Contributor: Sean T. Shallis, (201) 988-1393, sean@theshallisteam.com, www.stshomes.com

Contributor: Lawrence Yerkes, (609) 654-7300 ext. 206 or (609) 953-1330, foreclosures@timoninc.com, www.LawrenceYerkes.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 90–270 days

Notice of default: Required to notify borrower at least 30 days prior to initiating foreclosure

Notice of sale: 2 local newspapers, one of which is the largest municipality in the county or the county seat; posted on the property and in the county office; and given to the borrower at least 10 days prior to sale

Redemption period: 10 days

New Mexico

Contributor: Ron Campbell, (505) 821-7666, realtor3@ix.netcom.com, www.sherlockhomesnm.com

Contributor: Chris Kaplan, (505) 720-2624, ckaplan@KaplanNM.com, www.AboutThatHouse.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 120 days

Notice of default: Not required by state, but may be required by mortgage or deed of trust

Notice of sale: 4 consecutive weeks in a local newspaper, with the final notice appearing at least 3 days prior to sale

Redemption period: 9 months

New York

Contributor: Christine Forgione, (917) 939-1086, Nyhouses4sale@gmail.com, `www.Nyhouses4sale.typepad.com`

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial (more common) and nonjudicial

Process period: 210–450 days

Notice of default: Not required by state, but may be required by mortgage or deed of trust

Notice of sale: 4 weeks in a local newspaper

Redemption period: None

North Carolina

Contributor: Steve Whitfield, (336) 584-0347, steve@whitfieldproperties.com, `www.whitfieldproperties.com`

Contributor: Beth McKinney, (800) 251-3171, beth@budnbeth.com, `www.budnbeth.com`

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 90–120 days

Notice of default: Required

Notice of sale: 2 weeks in a local newspaper; mailed to the borrower at least 20 days prior to sale, with the last notice appearing not more than 10 days prior to sale; posted at the county courthouse at least 20 days prior to sale

Redemption period: 10 day

North Dakota

Contributor: Morris Pyle, (701) 238-1652, MorrisPyle@remax.net, www.FargoHomeCenter.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 90–150 days

Notice of default: 30-day notice of intent to foreclose

Notice of sale: 2 months in the county legal news, with the last notice appearing at least 10 days prior to sale; and delivered to the borrower

Redemption period: 180–365 days

Ohio

Contributor: Sam Miller, (740) 397-7800, Samsells@sammiller.com, www.SamMiller.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 150–210 days

Notice of default: Required

Notice of sale: 3 weeks in a local newspaper

Redemption period: None

Oklahoma

Contributor: Darryl Baskin, (918) 258-2600, info@darrylbaskin.com, www.darrylbaskin.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial

Process period: 90–210 days

Notice of default: Required

Notice of sale: 4 consecutive weeks in a local newspaper (in the county in which the property is located), with the first notice appearing at least 30 days prior to sale; and recorded in the county

Redemption period: None

Oregon

Contributor: Martha Hendrick, (541) 815-8300, Martha@Hendrick.com, www.Hendrick.com

Contributor: Tom and Patti Wilser, (800) 909-1091 or (503) 635-2660 ext 3905, TomAndPatti@TheThomasWilserGroup.com, www.HousesHousesHouses.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial

Process period: 150–180 days

Notice of default: Required 4 months prior to sale

Notice of sale: 4 consecutive weeks in a local newspaper, with the last notice appearing at least 20 days prior to sale

Redemption period: No right of redemption with advertisement and sale, up to 180 days for in-court foreclosure

Pennsylvania

Contributor: Nick Vandekar, (610) 225-7400 (office) or (610) 203-4543 (cell), Nick@VandekarTeam.com, www.VandekarTeam.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 90–270 days

Notice of default: Required 4 months prior to sale

Notice of sale: 3 consecutive weeks in a local newspaper and local legal newspaper; posted on the property at least 30 days prior to sale; and delivered to the borrower

Redemption period: None

Rhode Island

Contributor: Lisa Ranglin 223-6114 or (401) 465-3669, lisa.ranglin@cox.net

Deed type: Mortgage deed

Foreclosure process: Judicial (rarely) and nonjudicial

Process period: 90–270 days

Notice of default: Not required by state, usually required by mortgage

Notice of sale: 3 weeks in a local newspaper and local legal newspaper; with the first notice appearing at least 21 days prior to sale; borrower must be notified at least 20 days prior to public advertisement

Redemption period: None

South Carolina

Contributor: David Pautler, (800) 343-6821 ext 3006, pautlerd@hargray.com, www.TheDavidPautlerTeam.com

Deed type: Mortgage deed

Foreclosure process: Judicial

Process period: 150–180 days

Notice of default: Not required

Notice of sale: 3 weeks in a local newspaper and local legal newspaper; and posted at the county courthouse

Redemption period: 30 days, if lender reserves right to file a deficiency judgment; none, if lender waives the right

South Dakota

Contributor: Susan Raposa, (605) 391-5161 (cell) or (605) 342-1810, Susan@sellwithsusan.com or Susan@susanraposa.com, www.sellwithsusan.com or www.susanraposa.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial (more common) and nonjudicial

Process period: 90–150 days

Notice of default: Not required by state, but often required by mortgage

Notice of sale: 3 weeks in a local newspaper; and delivered to the borrower and any other lien holders at least 21 days prior to sale

Redemption period: 60–180 days

Tennessee

Contributor: Wayne Turner, (615) 590-4000, wayne@wayneturner.com, www.WayneTurner.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial (rarely) and nonjudicial

Process period: 60 days

Notice of default: Not required by state, but often required by mortgage

Notice of sale: 3 times in a local newspaper, with the first notice appearing at least 20 days prior to sale; although not required, the trustee often mails a notice to the borrower

Redemption period: Usually none, as specified in the deed of trust, but can be up to 720 days

Texas

Contributor: Michelle Cherry, (512) 695-8984, michelle.cherry@sothebysrealty.com, `www.CherryTeam.com`

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial (rarely) and nonjudicial

Process period: 30–90 days

Notice of default: Required

Notice of sale: Posted at the county courthouse; filed with the county clerk at least 21 days prior to sale; and mailed to the borrower at least 21 days prior to sale

Redemption period: None

Utah

Contributor: Jim and Billie Harsch, (435) 640-5106 or (435) 615-6638, jharsch@remax.net or billie@jimandbillie.com, `www.jimandbillie.com`

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 150 days

Notice of default: Required

Notice of sale: 3 consecutive weeks in a local newspaper, with the final notice appearing at least 10 days but not more than 30 days prior to sale; posted on the property at least 20 days prior to sale; and posted in the office of the county recorder at least 20 days prior to sale

Redemption period: Court decides; none for out-of-court foreclosures

Vermont

Contributor: Nancy Jenkins, (802) 846-4888, info@vt-homes.com, www.NancyJenkins.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial

Process period: 90–270 days

Notice of default: Required

Notice of sale: 3 weeks in a local newspaper, with the first notice appearing at least 21 days prior to sale; and delivered to the borrower at least 60 days prior to sale

Redemption period: 180–365 days

Virginia

Contributor: Frank Borges Llosa, (703) 827-0908, Frank@FranklyRealty.com, http://FranklyRealty.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 60 days

Notice of default: Required

Notice of sale: Delivered to borrower at least 14 days prior to sale; mortgage and state statutes may stipulate other advertising requirements

Redemption period: None

Washington

Contributor: Penny McLaughlin, (206) 842-2443, pennym@pennym.com, http://TalkToPenny.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial (more common)

Process period: 120 days

Notice of default: Required for out-of-court foreclosures

Notice of sale: Must be recorded at least 90 days prior to sale and mailed to the borrower and any other lien holders; published in a local newspaper at least once between the 32nd and 28th day prior to sale and once between the 11th and 7th day prior to sale

Redemption period: 12 months, unless redemption rights have been precluded

West Virginia

Contributor: Sarah Cooper, (304) 206-1457, WV.Agent@yahoo.com, `www.SarahCooperRealEstate.com`

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial

Process period: 60–90 days

Notice of default: Required for out-of-court foreclosures

Notice of sale: 2 weeks in a local newspaper, unless specified otherwise in the trust deed; mailed to the borrower and other lien holders at least 20 days prior to sale

Redemption period: 20 days

Wisconsin

Contributor: Jean Henning, (414) 384-1000, jean@jeansellsmilwaukee.com, `http://jeansellsmilwaukee.com`

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial (most common) and nonjudicial

Process period: 90–290 days

Notice of default: None, but the lender typically warns the borrower before filing with the court

Notice of sale: Varies according to court's ruling or county or local laws; in most cases, the property cannot be advertised for sale until 10 months following the court's ruling, although the lender and borrower can agree to an earlier date

Redemption period: 180–365 days

Wyoming

Contributor: Lisa Burridge, (307) 577-7775, Lisa@LisaBurridge.com, www.LisaBurridge.com

Deed type: Mortgage deed and deed of trust

Foreclosure process: Judicial and nonjudicial

Process period: 60–90 days, not including redemption period

Notice of default: Required to notify borrower at least 10 days prior to advertising the sale

Notice of sale: 4 consecutive weeks in a local newspaper

Redemption period: 90–365 days

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