Creating Wealth

WITH LITTLE OR NOTHING DOWN

Manual

The Nothing Down System of Creative Financing in Real Estate Investments

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SECTION A

Introduction

Robert G. Allen

M.B.A.

IN COOPERATION WITH

Richard J. Allen

Ph.D

PLEASE NOTE:

This manual has been prepared as an expression of the author's opinion concerning the subject matter covered. The information is from resources deemed reliable but not guaranteed. If legal advice or other expert professional service is required, the readers are urged to consult competent professionals, attorneys, accountants, etc. The author specifically disclaims any personal liability, risk, or loss incurred as a result of the application of any advice or information offered herein, whether directly or indirectly used.

Two Notes About Terminology

Throughout the text of this seminar workbook, the words "mortgage" and "trust deed" are used interchangeably. The precise technical difference between the two designations is made clear in the "Nothing Down Real Estate Glossary" included in the appendix. By practice, some areas will favor mortgages and other areas trust deeds (and still others use *both* instruments regularly); however, for the purpose of this seminar, it will be adequate to use the terms as equivalent and leave it to the seminar graduate to become acquainted with local patterns in such matters and seek competent professional advice where it is needed.

Concerning references like "real estate agent," "realty agent," "agent," and "Realtor®," the following convention has been adopted for this workbook: throughout the text, we use the term "real estate agent" (or just "agent" where the real estate connection is clear from the context) to designate the professional whose task it is to bring buyer and seller together and facilitate the completion of real estate transactions according to the principles of professional practice pertaining to the real estate profession. The term "Realtor®" is, technically speaking, not a generic term but a registered mark of the National Association of Realtors; a "Realtor®" is a real estate agent who, as a member of the NAR, embraces the ethical and professional standards adopted by the NAR. We urge graduates of this seminar who use the services of real estate agents to associate themselves only with the most experienced, creative agents who operate according to the highest standards of professional and ethical excellence.

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A Message from Robert G. Allen



Dear Student,

Welcome aboard! We hope to make the experience of this weekend a memorable one for you. For many of you, it will mark the turning point of your financial lifetime. We are committed to the following goals in bringing this seminar to you:

1. To teach you how to buy real estate with as little of your own money as possible.
2. To convince you to set specific and realistic goals for your financial independence.
3. To motivate you and give you the confidence to be able to buy your first piece of property within six months of completing the course.
4. To help you reach financial independence in the shortest possible time with the least amount of your own money.

So that we can both start out on the same foot, let me share with you what I call the "Nothing Down" philosophy:

THE "NOTHING DOWN" PHILOSOPHY

This is the "Nothing Down" IDEAL:

I IDEALISM

The purchase of real estate is not an end; it is simply a means to an end. It is a vehicle to take us to financial freedom quickly and safely. It is a way to help us overcome or eliminate the "money barrier" so that we can spend our precious time on the projects that are truly important to us. Once our real estate vehicle deposits us at the door of financial independence, we can get out and devote our time to more important matters. It is important, therefore, that we not lose our values along the way. We don't intend to teach you how to climb up to financial freedom by stepping on the backs of the unfortunate. Or to put it more simply, "For what is a man profited, if he shall gain the whole world, and lose his own soul?" or "What shall a man give in exchange for his soul?" Cicero said, "Without doubt, the highest privilege of wealth is the opportunity it affords for doing good."

We wish to emphasize the positive values of sharing, honesty, uniqueness, creativity, self-reliance, and hope. I hope that I can personally radiate these ideals to you.

D DISCIPLINE

We do not attempt to teach a course for the speculator. You can find plenty of that in the casinos of Las Vegas. Investing is a different process, a longer process. It requires patience. It requires commitment. It requires courage. It demands the self-discipline to be consistent in looking and learning. It may be necessary to forego luxury for the sake of an investment program. Saving money every month may be difficult, but it is necessary. We must learn how to set goals and stick to them.

E EDUCATION

Study is important, vital. Each new book on real estate investing offers at least one new idea that may prove effective in our program. Learning and practicing the basics is as essential to real estate investing as it is to golf or any other sport. As Derek Bok, president of Harvard University, has said, "If you think education is expensive, try ignorance!"

A ACTION

You have been a window-shopper long enough. It's now time to walk into the store and start buying what you have been looking at for so long. Don't you wish you had bought ten single-family residences ten years ago? You'll be saying the same thing to yourself ten years from now unless you learn how to act now.

However, it is also important to learn how to use your time wisely. "Efficient means *doing* things well. Effective means doing the *right* things well." This requires proper management of an investment portfolio to avoid "spinning your wheels" in improper action.

L LIBERTY

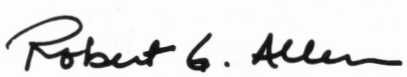
There is much more to liberty than just financial freedom. It is being free to reach your fullest potential in every aspect of your life. It is self-actualization. Think of these key liberating words:

LAUGHTER:	Fill your world with happiness. "Man is that he might have joy."—The Book of Mormon
LEADERSHIP:	Provide a better existence for your family.
LEISURE:	Freedom to pursue worthwhile goals.
LET:	Let the sun shine in.
LIFE:	Getting the fullest measure of it.
LIGHT:	Open up new vistas of fulfillment.
LOOK:	Look to the future with confidence.
LOVE:	Greater opportunities for sharing, caring.
LUCK:	Really only another word for successful, goal-oriented work.
LUXURY:	Within proper limits . . . why not?

This is the ideal of the "Nothing Down" philosophy. And mixed with the idealism is the realism of the investment world. It takes time to find the right deal. The hassle is sometimes not worth the profit . . . or at least it seems that way, especially when we get a midnight phone call from a tenant. There are the challenges of negative cash flow to contend with. There will be failures to learn from. It's all a part of the end result. And underlying the entire philosophy is the goal of Nothing Down: to buy real estate with as little of our own cash as possible. Nothing Down does not mean that the seller does not get cash. He just doesn't get *our* cash.

Good luck! And God be with you.

Sincerely,



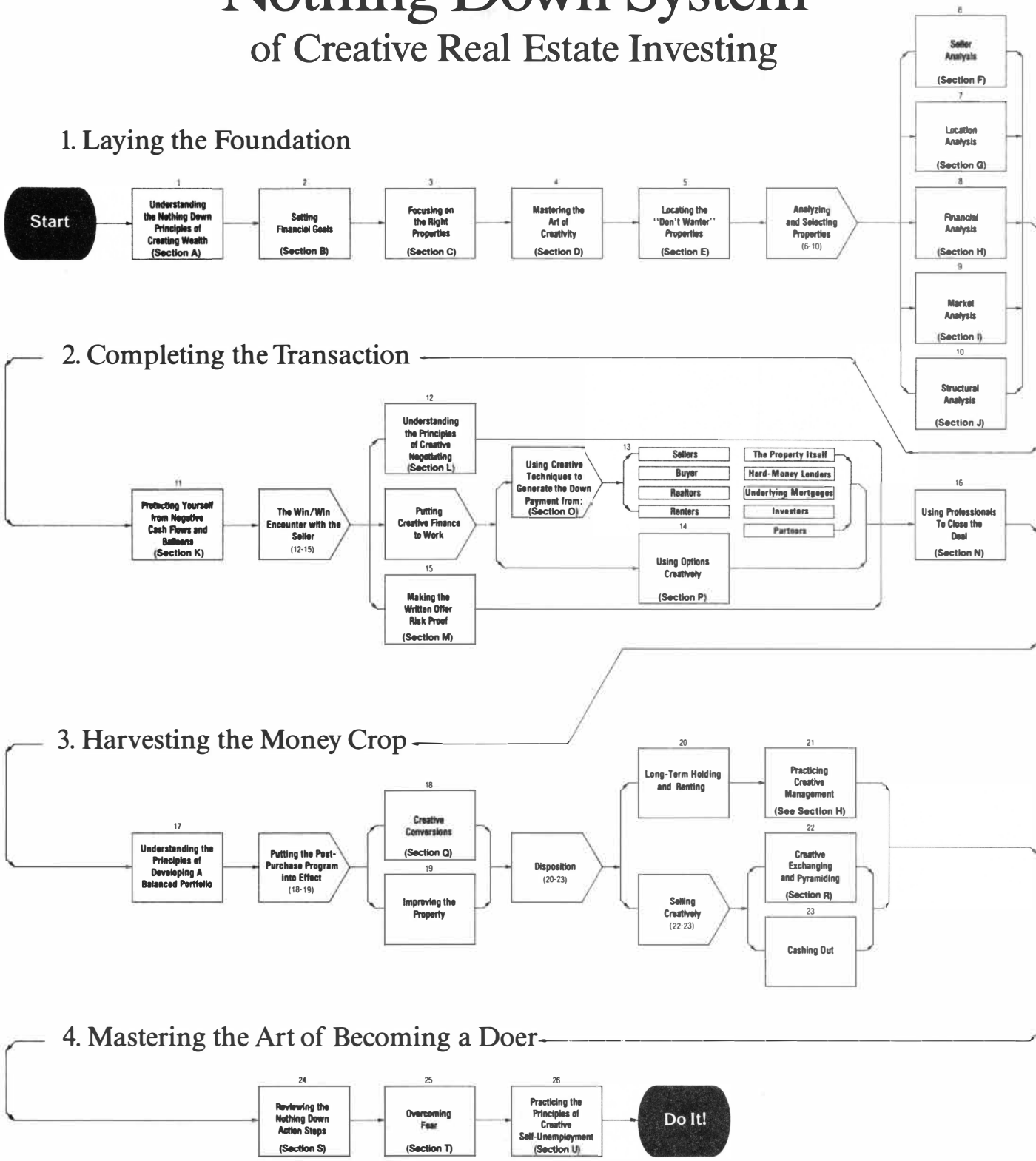
Robert G. Allen

"Money, which represents the prose of life,
and which is hardly spoken of in parlors without an apology, is,
in its effects, as beautiful as roses."

—Emerson

Note: The chart that appears on the next facing page is a roadmap to guide you through the material of the manual. The letter designations refer to the various sections of the manual. Study the chart carefully and keep it handy as you proceed through the material. The "Nothing Down" investment program is a logical step-by-step process. Each step reflected in the chart is essential and must be mastered.

Robert G. Allen's
Nothing Down System
of Creative Real Estate Investing



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SECTION B

Financial Goals

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Financial Goals: How to Set Them and Why They Are Important

B

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Financial Goals: How to Set Them and Why They Are Important

B

A. WHAT ARE YOUR FINANCIAL GOALS?

Take a few moments and write down your goals.

B. WE ARE A NATION OF DREAMERS

Most of us believe in a special kind of dream. People in the United States call it the "American dream." Canadians refer to it as the "Canadian dream." This dream states that any of us can get lucky. If we work hard enough and strive long enough and put in enough hours, we are going to become financially independent. We somehow assume that at the end of our lives after we have squandered all our money, there will be a secret safety deposit box filled with all the funds that we have filtered through our fingers throughout all those years. We see so many people on the beaches and the grass lawns of the universities and the boulevards of our streets with metal detectors hoping to find that big item—the lost diamond ring or rare or valuable piece of metal—and acting as if that is going to take them to their financial independence. Somehow I think we might assume that we are going to find a rare coin in our attic or that Aunt Sarah is going to leave us a half a million dollars or that we are going to locate a rare stamp in some of our lost possessions.

This is not the way financial independence comes. It comes when a person sits down with hard, careful planning and sets specific goals, charts in a specific course towards financial independence, and then has the courage to follow through on those plans no matter what the cost. It should be obvious to most of us that the so called "dream" does not work. Ninety-eight percent of those who have believed in our system are not financially independent as they reach age 65 because they did not analyze their situation and organize their goals and strive with definite purpose for financial freedom.

I once saw a television commercial of an older gentleman standing on the wharf watching a beautiful ocean liner go out to sea. In a very sad voice he turns and looks us squarely in the camera and says, as he thinks about that beautiful ocean liner going out to the ocean, "When I had the money, I did not have the time. And now that I have all the time in the world, I don't have the money." You see, he spent his entire life working for someone else and squandering his investments and all of his money so that when he reached retirement age, he didn't have any money left to do the kind of things he had lived his entire life dreaming about. That is not financial independence, and that is not the way to obtain it.

C. WHY GOALS ARE IMPORTANT

I firmly believe that this first half hour of our two days together is probably the most important. In our two days together, we are going to be giving you dozens and dozens of specific techniques for becoming financially independent, for being able to buy real estate with little or no down payment. Each technique is a tool, something we can use to help us reach our ultimate objective. What you find with so many individuals is that so few of them have specific written financial goals. So few of them read these financial goals once they have been written. And so few of them truly believe that these financial goals can be a reality. That is why I think goals should be discussed first, because they are the most important. If you have specific goals that you firmly believe can come to pass, then all the rest of our time together will be well spent. If you do not have specific written goals and you do not believe that they will come to pass, then your time will not be well spent.

1. The Hardware Store Analogy

Let me share an analogy with you. Suppose I were to send you to the local hardware store through the tool section of that store. You might look at the hammers and the nails, the saws, the power tools, the drills, and have a very

interesting time, educational perhaps, perhaps entertaining. But you would not be able to accomplish very much. If, on the other hand, I sent you back to the store with a specific goal in mind, such as "I want you to be able to build a doghouse within a 24-hour period of time," and if you were willing to accept that goal, then the series of events might happen a little bit differently.

First of all, you would go specifically to a certain section of the store. Rather than spending time analyzing and inspecting and window-shopping, you would go specifically to the tools that you would need, and all the others would be left. You would buy the saws and the hammers and the nails and the plans and the lumber and anything that was necessary. And then you would go directly home, build the doghouse, and be finished.

You and I are in the hardware store of life. Around us there are hundreds of ways to become financially independent, dozens of little-known secrets, thousands of books that have been written on the subject. If we don't have a specific written financial goal, we can spend our entire lifetime wandering and window-shopping without ever accomplishing anything. However, if we set ourselves a specific goal with a specific time limit to it and then go into the hardware store of life, everything starts to look a bit different. First of all, we set a financial goal to become a millionaire in a 15-year period of time. Like magic, things start becoming more important to us. As we read the newspaper, articles seem to pop right out of the newsprint and present themselves before us: "Here, read this. This is an article that talks about making money." We start noticing the books and start reading the articles that might help us become financially independent.

2. The Subconscious Mind

You will find that once you have completed this section and as you go home and in the weeks to come, if you follow these instructions explicitly, you will start noticing things that you have never noticed before. Ways of making money will come to you as they have never come before as your subconscious mind begins to become magnetized with your goal and with your desire.

Let's talk about the subconscious mind. I know this may sound a little bit unreasonable or slightly supernatural, but your subconscious mind is extremely powerful, extremely knowledgeable, and extremely capable of showing you solutions to all of the problems that you face. The subconscious mind works 24-hours a day, doing all of the kinds of things that your conscious mind does not wish to bother itself with. The subconscious mind handles breathing, it handles the digestion of food, it handles the healing of sores and sicknesses, it handles all of the transfers of blood from the different cells, and it is extremely powerful. Once the subconscious mind accepts an idea, accepts something that you really want, it begins to create ways to bring that idea into reality. But this has to be done in a very orderly fashion.

In a book titled *The Power of Your Subconscious Mind,* Dr. Joseph Murphy states, and I quote, "If you get into a taxi and give a half dozen different directions to the driver in five minutes, he would become hopelessly confused and probably would refuse to take you anywhere. It is the same when working with your subconscious mind. There must be a clear-cut idea in your mind. You must arrive at the definite decision that there is a way out, a solution. Only the infinite intelligence within your subconscious knows the answer. When you have come to that clear-cut conclusion in your conscious mind, your mind is then made up, and according to your belief, it is done unto you" (page 99).

In the book *Think and Grow Rich* by Napoleon Hill, he states, "More gold has been mined from the thoughts of men than has ever been taken from the earth." The reason for this is that when a person truly knows what

he wants and specifically writes it down and consistently pursues that goal, he will accomplish it. In our skeptical society we hear people say so often, "I'll believe it when I see it." This is exactly the opposite of what must be said. A person who believes in the power of the subconscious mind and his ability to reach a goal must say to himself, over and over again, "I'll see it when I believe it."

D. DETERMINE WHERE YOU ARE NOW FINANCIALLY

In order to help your subconscious mind process all the information that is necessary for it to give you the right solutions for your money problems, the subconscious mind needs to know where you are financially. Therefore, on the next four pages is a confidential checklist and survey of investment objectives. Although you may not have the time to fill this out now, do not hesitate to sit down after the course is over, when you have a quiet moment, and fill out this financial statement. This should give you a very clear picture of your financial health and help you understand what kinds of financial strengths and financial weaknesses you have. Pay careful attention to the budgeting section and make sure that you set aside enough money every month to go into a savings account. You would do well to read the very popular classic entitled *The Richest Man in Babylon* by George Clason.

E. DETERMINING YOUR LONG-RANGE GOALS

As you review your goals, how could you improve them? If I were a financial consultant and were to sit down with you as an individual, what could I suggest to you to make your goals more effective?

1. Basic Ingredients for an Effective Goal

a. Specific Date. Be realistic; give yourself at least five years. Anything less than five years may require a sacrifice of time, money, mental energy, and family togetherness that is so great that the price that would have to be paid would not be worth the result. Make sure that this specific date is perhaps even as specific as naming the day, the month, the year, perhaps even the time of day. It must be specific.

b. Specific Amount of Money. This should be stated in the specific amount of yearly cash flow from investments. In other words, when we think about financial independence, we generally think about becoming a millionaire, or having a half a million dollars worth of stocks and bonds, or owning ten homes and three vacation homes and six cars and three airplanes, etc. What financial independence really and truly means is being able to have enough money coming in on a cash flow basis yearly to support your lifestyle in the manner to which you would like to become accustomed and to have this yearly cash flow coming in steadily without having to work for it. Therefore, as you envision your ultimate financial independence, in a specific amount of time, you should also envision a specific amount of yearly cash flow: How much money do you actually need to have in order to retire and devote your time to other things? Is it $25,000 a year; is it $50,000 a year; is it $100,000 a year?

Once again, in determining this specific cash flow, you must not be too unrealistic; having a cash flow of a million dollars a year is probably not within the realm of most people's capacity, at least within a short period of time. Also, in determining this cash flow goal, you should take into consideration the effect of taxes and inflation on your long-term financial objective. If you wish to retire some ten years hence with $100,000 a year income, you must be aware that that $100,000 at that time may be worth

Confidential Checklist and Survey of Investment Objectives

SAMPLE

PERSONAL AND FAMILY DATA

Name _____ Date _____

Mailing Address _____ Phone _____

Employer/Position _____ Phone _____

Spouse's Employer _____ Phone _____

	Age	Date of Birth	Health	Occupation	S.S. # or Social Ins. #
Client					
Spouse					
Children					
Other Dependents					

	Firm	Phone
Attorney		
Banker		
C.P.A. or Accountant		
Insurance Broker		
Property Manager		
Other Financial Adviser		

When was your present will executed? _____ Spouse's? _____

Do you have a trust arrangement? ☐Yes ☐No Type _____ Trustee _____

INCOME AND TAXATION

	Self	Spouse	Total
Current Annual Taxable Income			
From salary, fees, bonuses, etc.	$	$	$
From interest	$	$	$
From dividends	$	$	$
From real estate	$	$	$
From capital gains (½)	$	$	$
Other (trusts, etc.)	$	$	$
Total taxable income	$	$	$

Expected future income? _____ When? _____

What income increases or decreases do you expect? _____

Do you receive additional non-taxable income? _____

Do you have a regular savings or investment program now? ☐Yes ☐No

Present monthly savings $_____ Could comfortably save $_____ monthly.

SAMPLE

TAX RETURN SUMMARY (LAST 4 YEARS)

	19_____	19_____	19_____	19_____
Adjusted gross income	$_____	$_____	$_____	$_____
Taxable income	$_____	$_____	$_____	$_____
Federal taxes paid	$_____	$_____	$_____	$_____
State ( ) taxes paid	$_____	$_____	$_____	$_____
Exemptions claimed	_____	_____	_____	_____

How many exemptions this year? _____ Estimated personal deductions $_____

Do you have any personal carry-over losses from last year? _____

Factors affecting future income _____

Comments _____

ASSETS AND LIABILITIES (EXCEPT INSURANCE)

Lender and Loan Number

REAL ESTATE

Type of Property & Location	How Acquired	Title Held In Name Of	Date Acquired	Adjusted Basis	Market Value	Amount of Mortgages	Present Equity	Monthly Cash Flow Before Taxes
				$	$	$	$	$
						TOTAL	$	$

SECURITIES (Listed and Unlisted)

Company & Type of Security	Registered In Name Of	Date Acquired	Cost Basis	Market Value	Margin or Loans	Present Equity	Annual Cash Flow Before Taxes
			$	$	$	$	$
					TOTAL	$	$

BUSINESS INTERESTS

Name of Company	Form of Organization	Date of Organization	Number of Employees	Percent Ownership	Client's Current Net Value	Client's Annual Net Income
					$	$
				TOTAL	$	$

SAMPLE

EMPLOYEE BENEFITS

Type of Plan Company	Tax Qualified?	Retirement Age	Retirement Benefits	Voluntary Contributions	Current Value	Death Benefit Now
Pension			$	$	$	$
Profit Sharing						
Savings						
Tax Sheltered Annuity						

LIFE AND HEALTH INSURANCE

LIFE INSURANCE

Company	Type	Date Acquired	Insured	Owner	Beneficiary	Face Amount	Cash Value	Loans	Annual Premium
						$	$	$	$
					TOTAL	$	$	$	$

MEDICAL AND DISABILITY INSURANCE

Type	Cancelled? Yes	Cancelled? No	Insurer	Insured	Periodic Benefit	Maximum Benefit	Exclusion	Annual Premium
Disability Income								$
Disability Income								
Hospitalization								
Major Medical								
Business Overhead								

FINANCIAL STATEMENT

ASSETS

Cash and checking	$_____
Savings accounts	_____
Real estate owned	_____
Securities	_____
Notes receivable	_____
Bonds — face value	_____
Furniture & personal	_____
Automobiles	_____
Life insurance cash value	_____
Net worth business	_____
Net lease value	_____
Boats, trailers	_____
Alimony	_____
Deposits on real estate	_____
Pension & annuity value	_____
Other_____	
_____	
_____	
_____	
TOTAL ASSETS	$_____

LIABILITIES

Mortgages	$_____	
Notes payable	_____	
Loans on life ins.	_____	
Debts, unsecured	_____	
Installment purchases	_____	
Property tax reserves	_____	
Income tax reserves	_____	
Long-term leases	_____	
_____		
_____		
_____		
TOTAL LIABILITIES	$_____	

NET WORTH $_____

SAMPLE

INVESTMENT OBJECTIVES

What priority do you assign to the following investment objectives?

_____ Additional current monthly income of $_____
_____ Capital growth/inflation hedge ☐ Short Term ☐ Long Term
_____ Tax shelter for ☐ Income ☐ Capital gain ☐ _____
_____ Professional management for ☐ Property ☐ Securities ☐ Trust
_____ Safety of investment
_____ Maintain minimum cash reserve of $_____
_____ Diversification of investment program
_____ Provision for family in event of premature death or disability
_____ Other

At what age do you anticipate full retirement? _____
What do you consider to be a minimum retirement income (today's dollars) $_____
What do you consider to be a comfortable retirement income (today's dollars) $_____
Comments (education funds, etc.): _____

COMMENTS

BUDGETING — Create your own wealth for pyramiding

Gross Income — including interest, dividends, rents $_____
Less deductions — Federal _____ Soc. Sec. or Soc. Ins. _____
State or Province _____ Others _____ (_____)
$_____

Spendable Income

		BUDGET	SPENT
1. Savings for investment = at least 10% of gross income			
2. Committed expenses:	a. Charitable		
	b. Housing		
	c. House maintenance		
	d. Utilities		
	e. Life insurance		
	f. Automotive		
	g. Medical		
	h. Others:		
3. Manageable expenses:	a. Food		
	b. Clothing		
	c. Personal expenses		
	d. Appliances		
	e. Furnishings		
	f. Building and grounds		
	g. Entertainment		
	h. Others:		

Total Expenses $_____
Spendable less expenses $_____

If there is income remaining, apply to your savings. If there is a deficiency of income, find ways to alter your expenses or increase income. Do not decrease savings!

approximately what $40,000 or $50,000 is worth today, depending on inflation.

Also, a word on retirement. So many people react negatively to what retirement means. Retirement is simply a state of mind. When a person reaches his financial goal, he is thereby able, if he so wishes, to quit his present job and devote the rest of his lifetime to doing the kinds of things that are important to him. It does not mean that he has to quit; it means that he is able to if he wishes to. Some people like to work, and work is important to them. To these individuals, part of their financial goal may be to have an income coming in at a specific level (dollar amount) while they continue to work and receive stimulation that comes from working with other people.

I also want to mention a word about the capacity of many individuals to even imagine the possibility of having a certain large amount of money coming to them every year without having to work for it. The first goal that I ever set for myself was to have $100,000 in net worth by the time I was 30 years old. I set that goal when I was 26 years old. At that time, I was going to college and living on an income of about $200 a month. This figure of $100,000 was such a large and incomprehensible figure to me that I almost hesitated to write it down. What most of us don't realize is that we are literally stuck in a rut of small thinking so that a figure of $100,000 or $200,000 or half a million dollars is almost incomprehensible to us. As our capacities to understand that goal increase, our goals also increase.

I can remember a time when having a goal of a million dollar net worth was totally unattainable in my view and now I have significantly increased my goals to even higher limits. We are consistently changing our goals as our capacity to understand them increases. Don't be afraid about setting a goal now that you do not seem to understand or comprehend. Your subconscious mind is totally able to comprehend these large figures and is completely powerful enough to suggest ways for you to reach your goals. What's more important now is not that you fully understand your goal but that you write it down and that you want it badly enough that your subconscious mind believes you and starts to help you accomplish it.

c. Specific Amount of Yearly Cash Flow. In the previous discussion of cash flow, you set a goal of obtaining a definite amount of cash flow each year. This cash flow has to come from the investments that you have been able to accrue to yourself over the period of your investing. A simple way of looking at your net worth objectives is to take your ultimate cash flow goal and multiply it by 10. In other words, if you wanted to retire in seven years with a net worth of $50,000 a year coming in from your investments, that would mean that you would have to have 10 times that amount in net worth: 10 × $50,000 is $500,000. If that $500,000 were invested in tax-free bonds, say, yielding 10 percent interest, then that would give you a $50,000 a year cash flow from your invested net worth. And this net worth would continually generate this $50,000 a year for as long as you left it in that specific investment.

d. Specific Plan of Action: The Gross Equity Appreciation Formula. Now that you have set a specific date, five to ten years hence, determined a specific cash flow that you would like to retire on, and multiplied that cash flow by 10 to determine the amount of net worth needed to generate this cash flow, you must next have a specific plan of action to follow to help you accumulate that net worth. This is done by looking on the next several pages at the two charts there: Gross Equity Appreciation Schedule and Gross Equity Accumulation Schedule.

(1) Gross Equity Appreciation Schedule. Let's look first of all at the Gross Equity Appreciation Schedule. This chart has been designed to show you how quickly real estate values increase and how quickly an investor in real

estate can accumulate a large net worth by buying property and holding it for future appreciation. For example, let's suppose that you are able to go out into the marketplace and follow the assumptions I have written at the bottom of the chart, i.e., that the values of properties you are purchasing are increasing by 10 percent a year, that all of your purchases are with little or no down payment, that there is no equity build-up (which is an assumption that we are going to have to make for the purpose of the chart, although it is not a true assumption since in most cases there will be equity build up), and that all the figures in the chart are rounded to the nearest or highest tenth.

If I were able to go out into the marketplace and purchase a quarter of a million dollars worth of real estate—perhaps a four-unit apartment building and maybe two or three investment homes—and hold that property for 11.6 years, the property would generate after that period of time $500,000 equity in it. The figures to the left of the chart in the Gross Value of Real Estate column show the gross value of the real estate that you are buying. The figures at the bottom of the chart are net equities that are accumulated.

Using the same example, how many years would it take a person who bought a quarter of a million dollars of real estate today to become a millionaire? You go to the left hand side of the chart and find a quarter of a million dollars and then you go along the column to the right until you find where the quarter of a million dollar column intersects with the bottom million dollar column, and that would be 16.9 years.

A note about inflation: All real estate that is well selected and properly maintained will increase in value in time. During the 1970s the average rate of appreciation on most rental properties was approximately 10 percent per year. At that rate of appreciation, a well-selected property would have doubled in value in just over seven years. The decade of the 1980s will continue to see appreciation on rental properties, but at much lower rates, at least for the foreseeable future. Depending on the rate of inflation, and the location, appreciation rates could vary between 5 and 15 percent in the next 10 years. The charts we include here show what a 10 percent appreciation can do. But even a 5 percent rate of appreciation can produce exciting results over a longer period of time.

(a) "How to Eat an Elephant"

Unfortunately, the Gross Equity Appreciation Schedule does not approximate reality. In other words, very few individuals will walk into the marketplace and purchase for themselves a million dollars worth of real estate all at once and then kick their feet up onto the table and wait for that to pyramid into a million dollars worth of equity. Most of us buy property one piece at a time. We have an elephant that we need to eat; we're going to eat that elephant one bite at a time instead of looking at the elephant and saying to ourselves, "My goodness, I could never eat that elephant." We must say to ourselves, "If I take one bite at a time, I can accomplish my goal." And, therefore, by looking at the next chart, the Gross Equity Accumulation Schedule, we can better understand how a long-range financial objective can be reached.

(2) Gross Equity Accumulation Schedule. The Gross Equity Accumulation Schedule is based upon the assumption that if a person buys one piece of real estate a year and holds that piece of real estate for the long-term, that this method of purchasing, over a period of time, will generate enough equity to take a person to financial independence. Let's make an assumption here. Suppose I had set for my goal to retire in seven years with a $50,000 a year cash flow coming in from my investments. How would I accomplish that goal? First of all, I have to say to myself, "If $50,000 a year is my goal, then how much net worth do I have to accumulate? $50,000 × 10 = $500,000. If I had a half million dollars in a bank somewhere generating 10 percent

GROSS EQUITY APPRECIATION SCHEDULE

Gross Value of Real Estate	Net Equity Columns								
$2,000,000	1.3	2.4	3.4	4.3	5.1	5.9	6.6	7.3	18.8
$1,750,000	1.4	2.7	3.8	4.8	5.7	6.5	7.3	8.0	20.0
$1,500,000	1.7	3.1	4.3	5.4	6.4	7.3	8.2	8.9	21.4
$1,250,000	2.0	3.6	5.0	6.2	7.3	8.3	9.2	10.1	23.1
$1,000,000	2.4	4.3	5.87	7.3	8.6	9.7	10.7	11.6	25.2
$750,000	3.1	5.4	7.3	8.9	10.3	11.6	12.7	13.7	28.0
$500,000	4.3	7.3	9.7	11.6	13.2	14.6	15.8	16.9	32.0
$250,000	7.3	11.6	14.6	16.9	18.8	20.5	21.9	23.1	39.0
	$250,000	**$500,000**	**$750,000**	**$1,000,000**	**$1,250,000**	**$1,500,000**	**$1,750,000**	**$2,000,000**	**$10,000,000**

Assumptions:

- Property values increase by 10% per year
- All of your purchases are nothing down
- Equity build-up is not counted in equity
- Figures are rounded to highest tenth

GROSS EQUITY ACCUMULATION SCHEDULE

Annual Accumulation	$250,000	$500,000	$750,000	$1,000,000	$1,250,000	$1,500,000	$1,750,000	$2,000,000
$300,000	3.5	5	6	7	8	8.5	9	9.5
$250,000	4	5.5	6.5	7.5	8.5	9	10	10.5
$200,000	4.5	6	7.5	8.5	9.5	10	11	11.5
$150,000	5	7	8.5	9.5	10.5	11.5	12.2	13
$100,000	6	8.5	10	11.5	12.5	13.5	14.5	15
$75,000	7	10	11.5	13	14	15	16	17
$50,000	8.5	11.5	13.5	15	16.5	17.5	18.5	19.5
$40,000	9.5	12.5	14.5	16.5	18	19	20	21

Net Equity Columns

Assumptions:

- Property values increase by 10% per year
- All of your purchases are nothing down
- Equity build-up is not counted in equity
- Figures are rounded to highest one half

NOTHING DOWN SEMINAR MANUAL

interest, I would have a cash flow of $50,000 a year. So my long range goal is to have a half million dollar net worth." I then go to the Gross Equity Accumulation Schedule, and I look at the bottom of the chart and find half a million dollars. That's what my goal is. Then I go up the chart until I locate the number of years that I have set for myself to become financially independent, in this case seven years. I go up to where it says seven years, and then I go over to the left, and I see the figure there of $150,000. What this means is this: if I purchase $150,000 worth of real estate each year in good areas over a period of seven years, and if that property appreciates at 10 percent a year, then at the end of my seven years of investing, I should have through appreciation alone over a million dollars worth of equity in the properties which I have purchased over that period of time. Naturally, appreciation rates above 10 percent will accelerate the process; appreciation rates below 10 percent will slow the process down so that the desired results may take a little longer. (In later sections we'll show you how to win even with zero inflation by buying properties 20 percent to 30 percent below market or by using the fix-up method!)

How to Become a Millionaire

Let's take another goal. Suppose I would like to become a millionaire. And I would like to be able to do it in approximately 10 years. How much real estate would I have to buy each year in order to accomplish that goal? First of all, we go to the bottom of the chart and find a million dollars in net equity. Then I go up the column vertically until I locate the number closest to my retirement, which is approximately 10 years, in this case 9.5, and then I go to the left to the column which tells me how much I have to buy each and every year to reach my goal. It's $150,000. If I want to accomplish my million dollar goal in seven years, I go up vertically from a million dollars until I get to the number seven and then over to the left until I get to $300,000 worth of real estate in order to reach my goal.

A Goal for the Less Ambitious

Suppose I don't have such ambitious goals. Suppose I want to give myself 10 years to have an equity of $500,000 so that I can retire and have a $50,000 a year cash flow. I go to the $500,000 net equity column, then go up vertically until I reach number 10, and then go to the left and find the figure $75,000. In other words, I would have to buy $75,000 worth of property each and every year consistently for the next 10 years to reach that particular financial goal, based upon the assumptions that I have set.

Breaking Down the Goal into Bite-Sized Morsels

If you use these charts carefully, charting out your long-range financial goals, you will find that they will help you in your mind to break down your huge, massive elephant of a goal into bite-size morsels. What most people don't seem to understand is that the purchasing of real estate is a very large investment and that having that fear of investing coupled with the knowledge that they are going to have to buy a massive amount of real estate generates an inertia that is almost impossible to overcome. We must get into the habit of breaking down our goals into small increments so that we can digest them. As we get out into the marketplace and are faced with the reality of the real estate market, we find that we may have to look for an entire year in order to be able to purchase one or two investments. In some years we may have dry spells where we might not be able to locate anything that we feel fits into our parameters of investing and within the goals we have set for small down payments, etc.

Persistence: Not What but How Much

The most important thing to understand is that a nothing down investor has to have patience. Sometimes nothing down investments come along in the first day of looking, and other times it may take 365 days of consistent, not just persistent, effort. Once we find our first piece of property to invest in, we

wait until next year to go out and buy our next piece of property. It's not what a person buys, but it is *how much* he buys—and *how consistently.* That is the most important thing you need to understand in your investment program: to work towards consistently buying property each and every year for a certain period of time. Don't get discouraged if you don't find something in six months. Many of our students have expressed concern over this, and they will find, as does almost every one of our graduates, that a feast or famine syndrome always occurs. You may go through six or eight months of famine without finding anything, and then you will go through a period of feast where you will find four or five or six pieces of property, and it becomes almost boggling. If you just adopt the attitude of a consistent searcher, you will succeed, because the numbers are on your side.

e. Write These Goals Down. Let's continue with our basic ingredients for an effective goal. If you have now set a goal for yourself and have set a specific date, a specific amount of money that you would like to have each and every year, and thereby a specific net worth that you must have to generate that cash flow, and if you have set down for yourself a specific plan of action by purchasing a certain amount of real estate each and every year, then write these goals down and read your goals at least once each day.

You will find included here a "Commitment Letter." This commitment letter is extremely important and must not be passed over lightly. This is where you are going to show your subconscious mind that you truly mean business about your setting of financial goals. Here it is that you formally acknowledge that you have adopted specific financial goals. This is the piece of paper that you will place on your mirror or in a conspicuous place in your home where both you and your spouse can be consistently reminded of what you have promised yourself to do.

Let's fill out this goal sheet together with a goal that I will choose as an example. Suppose you have decided that you would like to retire in seven years with a $50,000 a year net worth. This is how you would fill out your chart:

"I, Robert G. Allen, hereby acknowledge that I have formally adopted the following financial goals: on the _____ day of _____ , 19____ [which will be seven years, exactly, to the day from when you write this chart out], I will enjoy a cash flow of at least $50,000 a year. My net worth will be approximately 10 times this yearly cash flow or $500,000. If I so desire, I may announce my retirement from my job and devote time to do the things which are important to me, such as bridge tournaments or golf tournaments or giving aid to the needy or church work or charity work or watching television. In order to accomplish the above goals, I will have to purchase at least [go back to the Gross Equity Accumulation Schedule; look where it says $500,000 in the net equity column at the bottom, and you go up the chart to where it says seven years, over to the left where it says $150,000] $150,000 worth of real estate each year for the next seven years. My first purchase will be on or before _____ ."
[Six months from the day you write out this commitment letter. In other words, set that short-term goal for yourself. Don't let six months go by that you haven't purchased at least one piece of investment property.]

Signed this _____ day of _____ , 19____ .

Then have your spouse or your neighbor or someone whom you respect witness this commitment letter so that someone else is also knowledgeable of the promises that you have made to yourself.

f. Read Your Goals at Least Once a Day. Don't forget to read your goal at least once each day thereafter so that your subconscious mind can become magnetized to the goal which you have set for yourself.

g. Engage in Mental Imaging. The final and most important part of the setting of your goals is this: as you are reading your goals each and every day, you must engage in what is called mental imaging. This is the process of imagining what it would be like to possess the money that you are ultimately hoping for. Will you be driving a fancy car, will you be living in a nice home, will your family be taking vacations to far-away countries, will you be happy? View all these things in your mind and feel what it is like to possess that kind of money—not to have to work for a living, to be able to do the kinds of things that you would love to do for the rest of your life. As you feel these things happening in your imagination, your subconscious mind will become magnetized to the possibility of you reaching your financial goal. Good luck.

"Man's mind, stretched to a new idea,
never goes back to its original dimension."
—Oliver Wendell Holmes

COMMITMENT:

I, _____, hereby acknowledge that I have formally adopted the following financial goals:

On the _____ day of _____, 19_____, my net worth will be at least $_____. This will generate a yearly cash flow of approximately $_____. If I so desire, I may announce my retirement from my job and devote time to do the things which are important to me, such as _____

_____

_____

_____.

In order to accomplish the above goals, I will have to purchase at least $_____ worth of real estate each year for the next _____ years. My first purchase will be on or before _____.

Signed this _____ day of

_____, 19_____.

_____

_____

Witnessed by:

_____

Creating Wealth

WITH LITTLE OR NOTHING DOWN

Manual

The Nothing Down System of Creative Financing in Real Estate Investments

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SECTION C

Concentrating In Specific Markets

Robert G. Allen

M.B.A.

IN COOPERATION WITH

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Ph.D

Concentrating in Specific Areas Within the Real Estate Market

C

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Concentrating in Specific Areas Within the Real Estate Market

C

A. BASIC PARAMETERS FOR MAKING THE DECISION

Real estate is a large marketplace with hundreds of types of various investments, some with greater risk, some with lesser risk, some which require a greater degree of sophistication, others which require almost no sophistication, some which appreciate rapidly in value, others with a very small and sometimes negative appreciation in value. In all of this maze of investments and in the complicated analysis that is necessary to be successful, it is important to learn how to concentrate in the right areas. It's very important to learn how not to make mistakes. It's very important to take the precious time you have and make sure that it is spent in the right areas. The object and goal of our entire course is to get you to your financial independence in the quickest amount of time with the least amount of energy expended. I have invested in almost every area of real estate investments, and I have found that if one is not entirely careful, one can lose a lot of money as well as time. One of the most important principles to understand is why real estate goes up in value in the first place. And it all boils down to supply and demand. Let me illustrate.

Three wealthy old poker buffs were playing a very important game. The stakes were high, and after several hours of playing, the three of them had been dealt equally good hands. The antes increased, and finally each of them ran out of cash and began to gamble with the deeds to their various real estate holdings. The rancher from Montana began the last round of raises by pledging his entire 10,000-acre ranch, including all of his cattle and equipment. The oil baron from Oklahoma met the challenge by pledging all of his oil derricks and equipment. The wealthy Texan ended the bidding by offering his seven acres of ground in Texas.

"Seven acres!" gasped the other two partners. "Here we have pledged thousands of acres, and you expect us to accept your measly *seven* acres?"

"Yup," replied the Texan. "My land is right in the middle of downtown Dallas."

The point of the story is: some property appreciates faster in value than other pieces of property. What is important to understand with every property that you analyze is what is going to make this particular piece of property appreciate rapidly in value? According to the charts in the previous section, a 10 percent per year appreciation in property values will bring about dramatic results in our creating-wealth program. Some properties will appreciate at a higher rate, some at a lower rate, depending on location and economic factors. If this property is not carefully selected, we could undershoot our goals. Therefore, the questions that you need to ask yourself are: Does this property have a long-term potential for increase in value over the next 10 years? Does this property exist in a location and in general surroundings such that it will be in constant demand? Are there factors which make it less desirable than other properties at the present time? Is its neighborhood declining? Is there a possibility that it might decline in the near future? Does the property exhibit characteristics such as poor construction or unusual construction that might make it less desirable?

B. FOUR BASIC KINDS OF REAL ESTATE

Let's be even more specific. Let's look at all the various kinds of real estate and narrow ourselves down a little bit more. We can invest our money into four different kinds of property.

1. Undeveloped Land

That's land on the outskirts of civilization that has not yet been touched by any kind of development and is basically only good for holding the world together. The demand for this kind of property is not very great because it does not have any utility. And as for the supply, it is almost unlimited. Its potential for increase in value is probably not as great as other types of real estate.

2. Agricultural Land

Then we go into land for agricultural use. This type of land is not increasing extremely rapidly in value. It has a potential for negative cash flow because it does not generate quite enough income to support itself. As a story goes, a farmer went to his banker and took out $100 in one dollar bills and stood on the sidewalk of his small town and began selling one dollar bills for 75 cents to the first buyer. When someone came along and asked him what he was doing, he said, "Well, it beats farming." Purchase for farmland use is not a great investment.

3. Pre-development Property

The next kind of land is pre-development property—property that is in pre-development stages to go into another use, such as subdivision land and other types of land of this nature. This type of land is extremely lucrative to the sophisticated investor—the developer who is willing to take the risks that are necessary to do the changes that will convert a piece of farm ground or other "close in" type property into subdivision ground or commercial property or industrial property. It requires good financial backing, a strong sense of what is going on, the ability to deal with zoning and planning commissions, and the ability to handle an extremely complicated business. For that reason, since it is more sophisticated, I would highly recommend that our beginning investors do *not* start here—*do not buy land in pre-development stages*—not only because it requires sophistication but because it is extremely susceptible to one major problem that I call the *alligator principle.* The alligator principle is based on the fact that land does not generate income, but generally, in most cases, requires that an investor pay monthly cash flows to pay the taxes, interest, principal, and the other kinds of carrying costs. This means that the money comes out of your own pocket and ties you down to that investment. And since the money is necessary to keep this one investment alive, it limits the use of that same amount of money toward the purchase of another piece of real estate.

A real estate investment with a negative cash flow can wind up eating you alive.



A property with a negative cash flow is called an alligator. If a person does not feed his pet alligator its daily diet, month in, month out, then the alligator turns on him and eats him alive—the investor. I'm not saying that land in any of these pre-development stages or even raw ground or farm ground is not a good investment for the person who is sophisticated and knows how to handle the ins and outs of that type of investment. However, for the normal, ordinary, beginning investor, it is wise to stay away from these types of investments.

4. Urban/Suburban Land

Now there is another type of ground which is in the urban and suburban areas of our cities—in or close to populated areas or in small growing towns. This type of property is becoming increasingly in demand because of the forces of our population, because of the dream that every family should own

its own home. Subdivision properties are in demand for development. It is part of our growth scheme to keep on building and expanding, and therefore, there seems to be a constant demand for these kinds of properties.

C. CONCENTRATE ON INCOME PROPERTY

There are certain kinds of properties in urban/suburban areas which are better than others, and I will categorize them simply as income property. Income property is property with a structure upon it which can be rented out. Rent from the lease of this structure can go to help defray mortgage payments, taxes, insurance costs, and maintenance costs. These types of properties are:

houses	office buildings
apartment buildings	shopping centers
hotels	nursing homes
motels	commercial space
warehouses	mobile home courts
retail stores	

Any one of them is a good investment with a growing and stable economy.

D. FOR SAFETY, STICK WITH HOMES AND SMALL APARTMENT BUILDINGS

Rather than spending a lot of time discussing the negatives and positives, I have found in my search that houses and apartment buildings offer the greatest appreciation and profit potential for the future with the least amount of risks for the beginning investor. Briefly, the reason for this is that the supply of property seems to be favorable for the future, and the demand seems to be consistently increasing and promises to continue increasing throughout the next five- to 10-year period. When I bet my money into a real estate investment, I ought to be very sure that I'm betting my money in the safest place.

If I bet my money in a hotel or motel, a warehouse, a retail store, office building, shopping center, or any other kind of commercial endeavor, I am betting my money on things over which I have no control. I have no control over the economy of the country. As we know, it goes through various cyclical ups and downs. During a recessionary period those people who are holding retail stores or commercial office space for lease will find that businesses will start to fail, and they will be left holding buildings that are vacant, and which will be extremely hard to rent out. When you have a vacancy in a retail office space or a shopping center, you have a very large vacancy factor.

I like to bet my money on the surest possible thing. I like to bet my money on things which are necessary for my average tenant. If I bet my money on a home or apartment building, I am betting that a person who lives in my home or investment property has to be there and has no other choice. People have to live somewhere; they have to live in a house or apartment building, condominium, town home, trailer court, or a tent on the edge of some lake. But they have to live somewhere. Therefore, the odds are that even though we go through a dip in our economy, we are going to experience a lessening effect of the recession on our investment properties.

1. Supply and Demand

Let's talk about the supply and demand of houses and apartment buildings.

a. Homes. The supply of homes, of course, is directly affected by the number of homes that are being built in an area. There are several factors that are causing the supply of new-built homes to be increasing at a decreasing rate. The recent environmental pressures that have been placed on almost every city and community have caused the developer to have long delays in bringing new projects on line. This has been discouraging to the developer and has significantly increased the prices of many of the properties that the average person wants to buy. In addition, around most of our major cities, you will find the supply of buildable ground is rapidly diminishing. That is going to cause an upward pressure in the price of existing buildings as developers of new projects raise prices to assure a profitable venture.

During a tight money market, we find that tight conditions slow down the supply of existing new dwellings. At the same time that this supply is being slowed down, the demand becomes pent up behind the supply, which causes the prices to increase even more rapidly. I personally feel that the government's first priority at the present time is fighting inflation. It is going to be our experience in the next period of time to see a tightening of money. It's going to cause the demand to be built up or ballooned out of proportion to what it normally would be, because the supply is not adequate. It is important for an investor to take a look at the supply of properties in his marketplace and analyze the existing supply of houses in his area.

b. Apartment buildings. And about the supply of apartment buildings: the yearly need for additional new housing in the area of apartment buildings is not being met. The number of new on-line units that are coming on to replace or to fill up the need or the demand that is necessary is not nearly as large as the number of units that are going through demolition, abandonment, and condo conversion each year. This is causing an extreme shortage of apartment units in many of our large cities—some large cities have a less than 1 percent vacancy rate, and the national vacancy rate in recent years has been down around 5 percent, which is the lowest it has been in many decades.

In the early 1970s we had an oversupply of apartment buildings in many of the cities because the developers went out and overbuilt during a period of extremely loose money, and many of the apartment buildings in certain cities had high vacancy rates. You'll find that by and large this does not exist anymore and that the supply is not adequate to meet the demand for new housing. The reasons that this demand has built up all of a sudden for these existing apartment units are (1) condo conversions, (2) abandonment, (3) demolition, which has caused the number of units to shrink, and (4) the price of new homes, which has gone up significantly, forcing more and more people to put off the dream of owning their home.

I personally feel that the apartment outlook is extremely favorable for the next five years. Of course, it must be analyzed on a city-by-city basis. The first mortgage money to go in a tight money market is apartment money. It's the most difficult to find. The same is true of commercial investment money. Even when new apartment building money is available, it takes time to build—at least 12 to 24 months before a project comes on line after construction begins. In the meantime, the demand for apartment buildings is going to cause the rents to significantly increase, thereby causing the value of these properties to go up. I see that the future outlook in the supply and demand area of apartments and homes is extremely good.

2. Risk Analysis

Now let's take the next area of analysis, which is risk analysis. Of course, the risk of owning a home or apartment building as an investment is lower than

it is in any other type of investment. Why? First of all, the normal ordinary individual, having come up through the apartment and house-dwelling ranks, understands more adequately the renting out of a house or an apartment building. Most of us have purchased a home and understand the process of going through the closing and making mortgage payments. Most of us have rented something in our lifetime and understand the process of paying rents and the collection of rents and the paying of expenses, etc. This makes all of us at least partial experts in this field already. This is not the case with the renting out of shopping centers and warehouse space and commercial space. It's an extremely complicated field and has to be done carefully in order for a person to be successful at it.

3. Which to Choose: Apartments or Homes

This brings us to our next subject. If both houses and apartment buildings offer benefits, which should I choose? Where should I concentrate first? Why should I choose houses over apartment buildings?

a. In General: Not What but How Much and How Consistently. I have always said and I still maintain that it is not what a person buys in the real estate area as far as houses and apartment units are concerned, but it is rather how much that person buys and how consistently. How much do you buy each year? What is your particular goal? You must maintain a consistent pattern of purchasing properties each and every year without fail so that that compounding purchasing effect will lead you to financial independence. Therefore, when I go out in some marketplace to look for some piece of property, I'm not wholly concerned about whether it's a house or an apartment building. I buy the property from the first flexible seller I can find, and I put it in my portfolio.

There are relative benefits, however, to houses and apartment buildings.

b. Specific Factors to Consider.

(1) Size and Desirability of Homes. Houses have specific benefits. They are small; they are easy to understand. They are easily rented because they are more desirable to a renter than apartment buildings. Usually when families get larger, with two, three, or four children, they have to go to a home because they can't find an adequate or suitable three-bedroom apartment in the right kind of area. It is more desirable to rent a home because it's usually in good suburban neighborhoods, close to shopping centers, etc., and there are more desirable locations for homes.

(2) Management. In addition, there is one aspect that makes houses easier to manage: the tenant usually pays all the utilities. It is customary in apartment buildings that the landlord pays the water, sewer, and garbage; in the renting of homes, the tenant usually pays the water, sewer, and garbage and all other utilities.

(3) Liquidity. The houses are also purchased in smaller increments and, therefore, if a person finds himself with a portfolio of 10 houses and finds himself in a bind for cash, he can sell off one of his houses and raise the cash to solve his problem and still have nine-tenths of his portfolio still intact. But if a person owns a 10-unit apartment complex and finds himself in a shortage of cash and can't borrow it, then he has to liquidate his entire portfolio to solve his cash need, which means he may be faced with capital gains taxes and all the other problems that are inherent there.

(4) Rent Controls. Houses are usually exempted from rent controls in most cities, whereas apartment buildings (especially those over four units) may be subject to rent controls. Rent control mentality is sweeping the nation now in many of the major cities, and this is not going to be a diminishing problem but an increasing problem that we, as investors, should be aware of.

Another note on rent controls: if you find yourself in an area where rent controls will be a factor or are a factor at this present time, you may be wise to diversify into small investment properties. We've seen what's happened with rent control in New York City—it has caused the demise of hundreds of thousands of apartment units in that city, and this may be the case in several other cities. It is a very scary thing. There do exist advantages for profit by buying from people who are scared of rent controls and want to sell on good terms, but one should be extremely careful before proceeding into a rent control area.

(5) Flexibility of Sellers. The owners of apartment buildings are usually more flexible sellers than are homeowners. Homes are usually sold by people who have to buy another home. They need all their cash to go into another home. When you find an apartment building, however, you usually find a person who is a sophisticated investor who understands the ins and outs of real estate paper and understands that in tight money markets he has no other choice but to be flexible in his price and terms or he doesn't get his property sold. You will find more flexible sellers in apartment areas than you will in homes.

(6) Attaining Goals Quickly. When investing in apartment buildings, you also find that you can purchase large amounts of real estate in one single purchase, whereas in buying homes, you might have to purchase five or six or 10 or 15 different homes to accumulate the same gross value.

(7) Centralization. With apartment ownership, management can be centralized, costs cut, and expenses consolidated. It becomes easier to manage because you only have to go to one location to take care of the problems, where with a portfolio of homes you might have to go to several different locations.

(8) Cash Now and Appreciation. When we talk about apartment buildings, the opposite is true. When you buy the duplexes, four-plexes, or five-unit apartment buildings, you're going to find that since there has been such great demand for these kinds of smaller properties, the ability for you to rent out a four-plex or duplex for enough money to cover its mortgage payments is going to be extremely doubtful. The larger the apartment complex, the greater will be your ability to make and meet your mortgage payments from the rent that you collect, because of economies of scale. That does not mean that the larger apartment buildings appreciate as rapidly as the smaller ones. I still think the demand for smaller properties is going to continue because more and more people are becoming interested in real estate as witnessed by the number of people that are sitting in this room. And this will cause an upward trend in the prices of these types of properties. This does not mean you should not invest in larger pieces of investment property. It just means that there are benefits and detriments that have to be offset, that have to be analyzed.

Summary

Advantages of Houses

_____ Less complicated investment
_____ Generally in higher demand
_____ Can accommodate growing families
_____ Frequently located in more desirable neighborhoods
_____ Tenants usually pay all utilities
_____ Can be liquidated unit by unit if needed
_____ Generally escape rent controls
_____ Better prospects for appreciation
_____ Potential for higher quality tenants

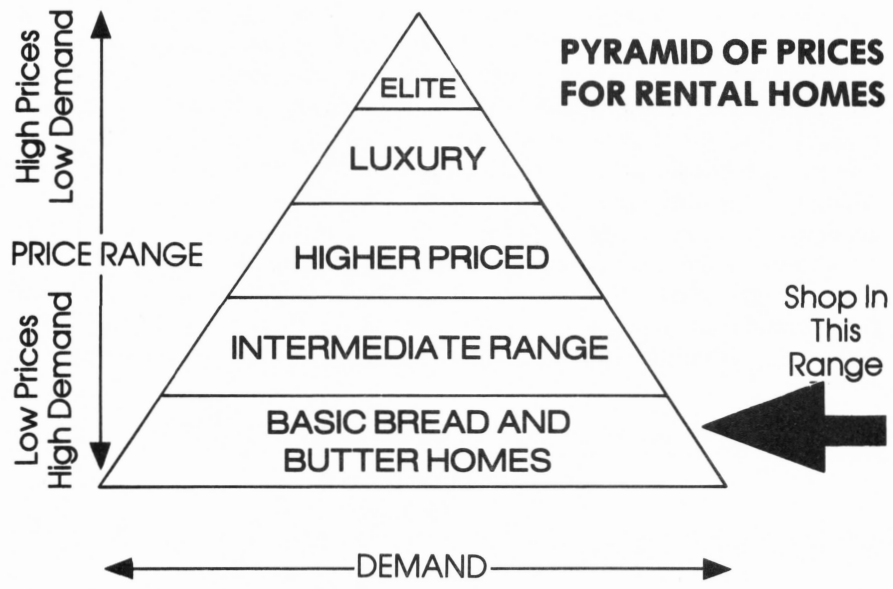
Advantages of Apartment Buildings

_____ Sellers generally more flexible and sophisticated
_____ Permit faster goal attainment
_____ Centralized management more efficient (economies of scale)
_____ Larger multi-unit properties have better chance for positive cash flow

4. Selecting the Price Range and General Location

Let's talk about the size of the areas that you want to concentrate in as you go into the real estate market. Each area is different.

a. Bread and Butter Properties. It is important to find a house that is located at the bottom of the pyramid of prices—the lowest priced acceptable house in the best acceptable neighborhood. (See figure.) We're looking for a working man's home—three bedrooms, carport, garage perhaps, basement if possible (although not necessary)—the general bread and butter type home with not a lot of frills. We are doing this because of the greater demand in that area. As more and more people want to own homes but get themselves pushed out of the price market, they have to stay along the bottom of that price pyramid. As you climb in the price pyramid and get into the more and more expensive homes, you'll find the demand is going to be less. Whenever we have ups and downs in the economy, these higher priced homes will become harder to sell, but the lower priced homes will always be available for government loans no matter what happens. They are your bread and butter type homes. They are also easier to rent out because that's what the normal, ordinary person is looking for.



What is the price range for bread and butter homes in your area?

b. Cash Flow Factors. As you stay in the lower priced homes in your particular area, you are going to have a greater possibility for a positive cash flow because rent will be commensurate with the small mortgage payment. The higher the price, the more difficult it will be for you to be able to rent that house out for enough to cover its mortgage payment. Therefore, as you inspect the houses, you should stay in the lower priced area.

c. Selecting the Best Community. Now some cities like Los Angeles, San Francisco, or Vancouver, B.C., where the medium income priced home may be upwards of $100,000, the probability of finding a home you can rent out without negative cash flow is almost zero. Therefore, you may even be wise to leave your own area and travel 50 or 60 miles to find lower priced properties. These are going to be the next booming towns. Each of you has to make the decision of where you are going to invest. There are still plenty of possibilities of making money in any city no matter what the prices are. Real estate increases in value because of supply and demand. Choose an area where there will be consistent, steady demand throughout the length of your ownership.

5. Diversification

This discussion of houses and apartment buildings should not lead you to believe that I have had any great love for one over the other. I do believe in a diversified portfolio spreading your marbles in as many baskets as you possibly can. Apartment buildings have a greater potential for a condominium conversion, so there are benefits and detriments in each kind. Therefore, remember: it is not what you buy but how much you buy and how consistently. As to diversification, you should always maintain a portfolio of several homes and several apartment buildings to take advantage of the benefits of each.

As a summary of this particular section, let it be remembered that houses and apartment buildings offer the greatest potential for the future, with the least amount of risk. And that is where you should concentrate. One last word for the person who does not wish to heed my advice but has already a certain amount of expertise in other types of properties, such as shopping centers, warehouses, and commercial space. If you feel that your expertise is enough to warrant your investing there, don't let my advice stop you. I'm generally, predominantly, speaking to the beginning investor who wants to be able to do the most amount of investing with the least amount of risk. There is generally more money to be made in shopping centers and commercial spaces and development of land. But there is also risk that goes with it. If you don't know what you're doing, you can lose everything.

"I am diversified
heavily into real estate!"
—Robert G. Allen

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in Real Estate Investments

SECTION D

Mastering The Art Of Creativity

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Mastering the Art of Creativity

D

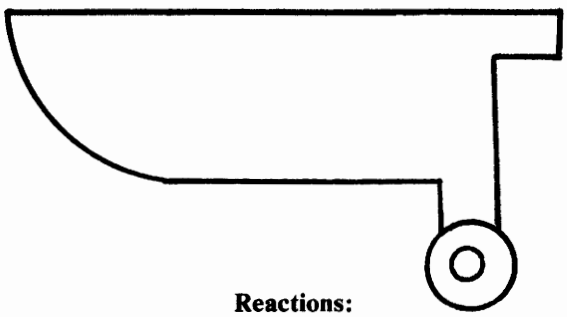
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Mastering the Art of Creativity

D

A. TAKE A C.Q. (CREATIVITY QUOTIENT) TEST

Try your hand at this one. Below is a proposed new model for a wheelbarrow. Write down your first three reactions to this idea.



Reactions:

1. _____

_____

2. _____

_____

3. _____

_____

If you are like the average person, you might have listed some perceptive reasons why the wheelbarrow design is problematic, e.g., "The wheel is too small," "The wheelbarrow is poorly balanced," "The handle is too short," etc.

In the conventional sense, you are absolutely right. And yet it is possible to look at the wheelbarrow design in a different and creative way. Note these possible responses:

"Hey, that's neat! You could put a trap door in the bottom of the hopper and dump out the contents over a cliff more easily than with a regular wheelbarrow."

"Very interesting proposal. A beachcomber could make good use of this wheelbarrow by walking behind it in shallow water and using it as a kind of traveling storage vessel for the objects he finds."

"Because of the shorter handle and smaller wheel, this model would be much easier to ship," etc.

Get the idea? These last responses don't zero in on the negative aspects of the design but begin to look for its unique and positive features and for its potentially novel applications. Of course, the creative ideas need to be

analyzed and tested in reality, but the point is: they move us in a positive and creative direction.[1]

B. WHAT IS CREATIVITY?

Generally speaking, creativity is the ability to solve problems in new and productive ways. Consider the following illustration:

1. The Parable of the Creative Dervish

Once upon a time, three Arabian brothers inherited 17 camels with the stipulation that the oldest brother get one-half of the camels, the second brother one-third, and the youngest brother one-ninth. The trouble was: they could not divide up 17 camels in this way. Hopeless situation, right?

Wrong! Just at the point when hostility was about to break out among the brothers, a creative dervish rode up smiling on his camel, listened to their story, pondered the problem intensely for a good while, then while sipping a cool drink of desert dew, came up with a flash of creativity. He had the solution.

Before we let you in on it, put on your thinking cap and try your hand at creativity.

My Solution:

_____

_____

_____

_____

Still stymied? Here is what the dervish did. With a playful smile, he added his camel to the bunch, making 18 in all. Then he instructed the oldest brother to take one-half of them (nine), the second brother one-third (six), and the youngest brother one-ninth (two). The delighted brothers walked away with a total of 17 camels (9 + 6 + 2), the same number they had inherited.

And what of the one camel left over? The creative dervish mounted that one (it was his own), and with a twinkle in his eye, rode off into the desert sunset.

2. The Nature of Creativity

Much has been written about the nature of the creative process, but the parable illustrates the essential points:

a. A Special Way of Looking at Things. Creativity is an ability to look at a situation in a novel or ingenious way, unhampered by the customary way of perception.

"Genius, in truth, means little more
than the faculty of perceiving in an unhabitual way."
—William James

b. A Special Way of Organizing Things. It is an ability to combine resources in new and productive ways.

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[1] The wheelbarrow illustration is based on an example from the excellent little book by David Campbell, *Take the Road to Creativity and Get Off Your Dead End* (Niles, IL: Argus Communications, 1977), pp. 9-12.

"To create consists
precisely in not making useless combinations
and in making those which are useful and
which are only a small minority.
Invention is discernment, choice."
—Poincaré

This aspect often takes the form of seeing novel uses for things. It took the dervish to perceive that his camel (his means of transportation) could also be used temporarily as an arithmetic unit (the eighteenth camel) in order to solve an accounting problem.

c. A Special Attitude. The creative individual always operates in an atmosphere of positive thinking and hope. Instead of saying, "It cannot be done" or "That's not how we do things," the creative individual says, "Aha! Let's try it this way." The creative spirit is an independent and hopeful spirit. It is the patience to suspend judgment or to defer closure which is critical to the attitude of a creative thinker.

"Inspiration favors the prepared mind."
—David D. Edwards

d. A Special Commitment. Like the dervish, the creative individual does his homework, looks at all the alternatives, invests all his energies and faculties, and does not give up until he has come up with some solutions. Each real estate transaction consists of a series of hurdles. Each hurdle must be overcome. We have to have the stamina to stick to our task even though the hurdles seem insurmountable. I don't want you to die of thirst just inches from the fountain.

e. A Special Spark of Life. The creative individual not infrequently has a twinkle in his eye, a sense of play, a lively exuberance, and then an ability to detach himself after much hard work and relax—have fun—put himself at ease and into that frame of mind where the flash of inspiration bursts in upon him, and everything suddenly falls into place.

3. The Barometer Story: A Further Illustration

The process of creativity is a mysterious and interesting one. It is brilliantly described in this story. The story deals with a student who refused to parrot back what he had been taught in class. When the student protested, Mr. Calandra was asked to act as arbiter between the student and his professor:

> I went to my colleague's office and read the examination question: "Show how it is possible to determine the height of a tall building with the aid of a barometer."
>
> The student had answered: "Take the barometer to the top of the building, attach a rope to it, lower the barometer to the street, and then bring it up, measuring the length of the rope. The length of the rope is the height of the building."
>
> A high grade is supposed to certify competence in physics, but the answer did not confirm this. I suggested that the student have another try at answering the question. I gave the student six minutes, with the warning that his answer should show some knowledge of physics. In the next minute he dashed off his answer, which read:

"Take the barometer to the top of the building and lean over the edge of the roof. Drop the barometer, timing its fall with a stopwatch. Then, using the formula $S=1/2at^2$, calculate the height of the building."

At this point, I asked my colleague if he would give up. He conceded, and I gave the student almost full credit.

In leaving my colleague's office, I recalled that the student had said he had other answers to the problem, so I asked him what they were. "Oh, yes," said the student. "There are many ways of getting the height of a tall building with the aid of a barometer. For example, you could take the barometer out on a sunny day and measure the height of the barometer, the length of its shadow, and the length of the shadow of the building, and by the use of a simple proportion, determine the height of the building."

"Fine," I said. "And the others?"

"Yes," said the student. "Take the barometer and begin to walk up the stairs. As you climb the stairs, you mark off the length of the barometer along the wall. You then count the number of marks, and this will give you the height of the building in barometer units. A very direct method.

"Finally," he concluded, "There are many other ways of solving the problem. You could go down to the basement and knock on the superintendent's door, and when he answers, you speak to him as follows: 'Mr. Superintendent, here I have a fine barometer. If you will tell me the height of the building, I will give you this barometer.'" (Alexander Calandra, *The Teaching of Elementary Science and Mathematics).*

Creativity is born when you have a problem to solve. And as you can see from the above story, there are many ways of solving a problem. Creativity is the art of looking for solutions that are out-of-the-ordinary, different, and unorthodox.

C. ROADBLOCKS TO CREATIVITY

These roadblocks must be removed from an individual's lifestyle in order to experience the maximum creative power.

1. Fear of Looking Foolish or of Failing

Creative persons know that failure is only one more step on the way to success.

"Asking questions,
which is essential to creativity,
means laying your ignorance out in the open."
—David D. Edwards[2]

2. Tendency to Judge Quickly

Create ideas first and then weed out the less practical solutions. There's plenty of time for judgment. You are already a strong criticizer. Try being a creator instead.

---

[2] See the useful little book by Edwards, *How to be More Creative* (Mountain View, CA: Occasional Productions, 1978), p. 20.

3. The Need to Conform

Society will frown upon all new creative ideas. You must be willing to go against the current—to challenge conventional thinking. Don't let someone tell you what is right and wrong.

4. Inadequate Information Gathering and Processing

Solutions multiply with information. Like a kaleidoscope, the more you turn the information over in your mind the more solutions are found.

5. Inability to Perceive the Correct Problem

Don't solve a headache with brain surgery where an aspirin would have been sufficient.

D. WHAT ARE THE IMPLICATIONS OF CREATIVITY FOR THE ASPIRING "NOTHING DOWN" INVESTOR?

The approach and techniques described in the seminar go beyond the usual patterns of real estate investment; they are what might be called creative, that is, innovative, new, unconventional. They also work well, which makes them essential tools for the layman to use.

How You Fit In

The "Nothing Down" System is dynamic. Not only will you be mastering the creative techniques described in the seminar and workbook but you will also be adding creative techniques on your own—ideas and variations that you develop yourself to fit the investment circumstances you encounter. Many of the ideas in the "Nothing Down" System have been and are being contributed by graduates of the seminar, people like yourself. There is nothing like a desire for financial independence to bring it out! The following points will summarize the implications of creativity for the "Nothing Down" investor:

1. Be Curious and Questioning!

"The creative process starts with a question" (John E. Arnold in *Education for Innovation*). In order to define the correct problem, you need lots of information.

2. Have Confidence in Yourself!

There is more creativity in you than you realize. If you are new to the investment field, all the better. Your fresh, unencumbered perspectives are an asset to you.

"True genius is always accompanied with good sense."
—Boswell

3. Study!

Immerse yourself in the full range of techniques and examples given in the seminar and workbook. Read additional recommended materials whenever you can. Imagination receives its power to create from a saturation of knowledge.

4. Reach Out!

Participate in the ACRE Group activities in your city. Ask questions of your professional contacts. Note the variety of creative approaches being used.

5. Be Persistent!

It might take you 50 contacts to find a don't wanter to suit your conditions and practice your ultimate measure of creativity on. But it is worth it. And it will no doubt take much effort and ingenuity in coming up with the combination of creative techniques powerful and effective enough to close the deal. Remember that each step brings you closer to financial independence.

6. Be Unique!

Financial independence comes most readily to the person of independent spirit. Don't let the criticisms of the crowd of traditionalists around you get in the way of your ingenuity.

"When a true genius appears in the world,
you may know him by this sign,
that the dunces are all in confederacy against him."
—Jonathan Swift

7. Be Positive! Thousands are finding their way to financial independence with "Nothing Down" techniques. You can do it, too—with creativity and hard work.

8. Have Fun! Relax! It is exhilarating. Enjoy your interactions with people. Play with ideas. Cultivate the creative sparkle in the eye. It's part of the game.

E. TRADITIONAL APPROACHES VERSUS CREATIVE APPROACHES

Study the following contrasting statements as illustrations of the creative spirit of the "Nothing Down" System of investments. Details will follow in later chapters.

Conventional Wisdom	"Nothing Down" Wisdom
To sell something, you must first own it.	To sell something, you must first have an "interest" in it.
To satisfy a seller, you must first determine how much cash he wants for his equity, then give this amount to him.	To satisfy a seller, you must first determine what he wants, then get it for him, whether it is cash, property, a trip abroad, or just relief from a property he no longer wants.
The buyer and seller must of necessity approach each other as adversaries.	Find a "don't wanter" seller whose problem you can solve, and he will be your friend from the beginning.
There is not a better person to negotiate with the seller than the real estate agent himself.	There is no better person to negotiate with the seller than the creative real estate buyer himself, or a creatively trained real estate agent who represents him as a buyer's broker.
Be careful: your purchase is for a lifetime.	Be careful: your purchase is for a lifetime, or perhaps for two days, whichever results in the greatest benefit to you.
When you buy, judge the property for what it is.	When you buy, judge the property not only for what it is but for what it might be converted to.
To buy from a distressed owner at a discount is to take advantage of him.	To buy from a distressed owner at a discount is to solve his problem.

All real estate transactions must have a down payment in cash.	When a down payment is required in a transaction, it might be in the form of cash, paper, property, professional services, or any consideration that might be of value to the seller, subject of course to local statutes and legislation.
When gathering information about a property, be courteous and tactful: ask the seller only general questions.	When gathering information about a property, be courteous and tactful but ask any question that will be of help to you in the transaction.
When a seller responds to your questions, he conveys facts about the property.	When a seller responds to your questions, he conveys facts about the property but more importantly about himself: his attitudes, his flexibility, his openness to creative ideas, his degree of being a don't wanter.
When you need cash for a transaction, either use your own or borrow some from a bank.	When you need cash for a transaction, use your own funds or bank funds only when you absolutely have to; preferably borrow funds from all the others involved: the seller, the real estate agent, the renters, the holders of underlying mortgages, a partner, even the property itself.
Borrowed funds must be repaid in specific fixed installments of principal and interest at a steady rate.	Borrowed funds may be repaid in any mode acceptable to lender and borrower (variable interest, balloon payments, interest only, etc.). Potential combinations are limited only by the imagination.
When the deal is closed, the buyer walks away with the deed, and the seller walks away with cash.	When the deal is closed, the buyer walks away with the deed, and the seller walks away with paper. Sometimes the buyer also walks away with cash in his pocket.
In order to obtain mortgage money from hard-money lenders, you need to have (1) cash down, (2) good credit history, (3) strong financial statement, and (4) a good, steady job.	In order to obtain mortgage money from hard-money lenders, you need to have these four things or be linked with someone who does.
When you retire at 65, you will have a gold watch.	When you retire in five to 10 years, or sooner, you will have financial independence.

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in Real Estate Investments

SECTION E

How To Find The Bargain

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How to Find the Bargain: The Don't Wanter Seller

E

A. THE DON'T WANTER SELLER

There is a theory about people who are owners of real estate which holds true no matter where you live, no matter how tight your real estate market is, no matter how quickly the properties are selling in your area, and that is the theory of the "don't wanter seller."

A don't wanter is someone who, because of circumstances in his life, has to be or wants to be flexible in either price or terms when he sells his property. At this very moment, in this very city, there are people who have to sell their real estate or who want very much to sell their real estate. Of those people who are attempting to sell their real estate at this present moment, perhaps 90 or 95 percent of them are not even interested in being flexible in price or terms. These people are wanters. They are going to be hard-nosed to deal with. They want their price, perhaps because they have an appraisal, or they want their terms. They want all cash. They dictate the way the negotiation will go, and you are just another buyer. It is no fun to deal with someone who has this attitude. For that reason, we avoid that type of person as much as possible. And 90 to 95 percent of the time in looking for properties as soon as we notice the person is not flexible, we automatically and cordially dismiss ourselves and start looking for someone who is going to be flexible.

And in 5 to 10 percent of the cases, as you do your preliminary looking for a seller, you will notice that the seller has certain problems that he has to have solved. There are certain circumstances that have come up in his life that make him become flexible in the way he is willing to sell his property. There are at this very moment thousands of people, right here in this city, who would love to sell their real estate and be flexible about it. It is our job as an investor to find those people and to learn how to negotiate with them so that we can solve their problems and so that they can solve ours. We solve their problems by buying their real estate from them, and they solve our problem by letting us buy that real estate in such a way as to make it easier for us to get in with little or none of our own money.

1. Case History

Let's examine this don't wanter seller by looking at the following case study. Circle all of the red flags you see. What are the clues that you find in this particular example that indicate to you that this person is a don't wanter?

The Don't Wanter Seller: The Foundation of Creative Financing

Have: Ten-unit apartment building located at approximately 50 miles northeast of and 250 miles southwest of _____ . Fully furnished and totally vacant!

Price: $45,000

Loans:	$23,000 payable at $285.20 per month, including interest at 8.5% per annum. Assumable or take over. No Qualifying.
Equity:	$22,000
Why does not want:	This is a newly-acquired property. While still in escrow, the client received a job offer he couldn't refuse in another area of the country. He cannot properly manage property.
Wants:	Will exchange for land, paper, construction equipment, or personal property. No geographical limitations.
Contingencies:	1. Present owner will lease back at $285.20 per month, until occupancy reaches 60 percent or for one year, whichever comes first. 2. Counselor will assume responsibility to obtain resident manager on or before possession date.
Remarks:	This property is listed at 33% below market value due to the vacancy situation. This is a good opportunity for an individual with initiative and ability to solve problems. Local officials are expecting a construction boom and massive housing shortage in the area in the near future due to extensive energy exploration and construction of a mineral processing plant.

2. Two Varieties of Don't Wanters: Retailer and Wholesaler

Now that we've had a chance to examine an actual case history of a don't wanter, let's take time to examine all of the reasons that cause people to become don't wanters. There are approximately 20 reasons—20 occurrences, 20 circumstances—which, when they happen in people's lives, may make them want to sell their real estate and may make them become flexible in their price and terms.

Now there are two general types of don't wanters. There is the don't wanter who, first of all, is selling his property at retail. He will be flexible only in his terms. For example, you might find a fellow who needs to sell his property because he just can't stand the management any longer or who refuses to take a cut in price because he wants to make his paper profit. Just to get the problem off his hands he will be more than willing to sell to you with little or no down payment. On the other hand, you have another kind of a don't wanter. And that's the don't wanter who wants to get rid of his property but has to sell in order to raise cash for solving certain money problems. This type of purchase is what I call the wholesale purchase because if he is going to be inflexible in his terms, which means he wants all cash, then he's going to be very flexible in his price. And that means that I'm going to offer him a lower than market price and give him all cash. Either way, I win. I either buy a property at full retail price and maybe even above retail with no down payment at all. Or I buy a property at 15 or 20 or 30 percent below the market price using a lot of cash and know I'm making money on the way in and place considerable cash into it. Either way I am investing and not speculating.

B. TWENTY REASONS FOR BECOMING A DON'T WANTER SELLER

Now for the 20 reasons that cause a person to become a don't wanter:

1. Divorce

Divorced couples frequently have to dispose of their real estate holdings to split up the estate. In many such cases, those persons who end up with the property cannot make the payments by themselves or find themselves in a situation where they can't stand the property because of the bad memories that were involved there. And they may find themselves in a circumstance where they will be more than willing to be flexible to get out of that piece of real estate.

2. Obsolescence

The next type of don't wanter is a person who has an older type building that requires severe or extreme remodeling to bring it up to current standards. Perhaps it needs fire walls or fire doors or expensive fire escapes to bring it up to present code. And he says to himself, "I think I'd rather dump this property than have to go through the expense and the hassle to fix it up."

3. Negative Cash Flow (Alligator)

The next don't wanter is the person who is suffering from an alligator. This person bought a piece of real estate without doing his checking and finds that he now has an alligator on his hands. He rents it out; he makes his payments, and his payments are larger than his rent, and every month he forks out $200 out of the money that he cannot afford. So his wife says, "If you're going to take money out of our family budget to feed your apartment building (pet alligator), then this has got to stop." And he finally says, "Okay, I'll sell. Let's get out of it as quickly as we can."

4. Transfer

In many cities where a lot of turn-over occurs in certain jobs, such as the armed services, political appointments at a national level, high-level sales positions, etc., you find the situation where people are given orders to move to a new job. Consequently, they have to be at their next place of employment within a very short period of time, and they don't have the opportunity to sell on a long-term listing. In many instances, their company pays for their transfer. And in many instances, the company pays for the loss that they might have incurred because of the fact that they had to put their property on the market and sell it quickly. We can step in and perhaps pick up a very excellent piece of property at a good, low price because of the circumstances involved.

5. Wrong Management Approach

The most important and largest contributors to don't wanterism are management problems. We might find a neophyte investor, an enthusiastic person who knows that he can become financially independent by investing in real estate, so he runs out and reads the books and goes out and buys himself a couple of pieces of real estate, and he quickly learns that it's not quite as easy as he thought it was. Perhaps he buys a little duplex somewhere in the city without really testing the location and then finds that this location draws the wrong kind of tenant. Soon he begins to realize that he's taking on the entire welfare system of the country, that his tenants begin to take advantage of his kind-hearted approach to management, and soon he finds that they're late in their payments. He finds that their motorcycle payment was more important than the rent and that the trip to California to visit Disneyland was more important than the rent, and he starts to pull money out of his own pocket to feed his mortgage payments. Then one morning he goes down to collect their rent and finds that both the units are vacant, and two of the people have left in the middle of the night owing substantial amounts of rent. With no hope

of ever having an opportunity to collect this rent, he says to himself, "If this is the road to riches, I'd rather be poor and happy than rich and miserable." Now what that person ought to understand is that management is an extremely important skill and that it's a very, very important part of how to become financially independent. We can't just leave it to chance. As you are checking in the marketplace, you will find dozens and dozens of people who don't understand management and who are willing perhaps to get out of the hassle it has caused them.

6. Arrears in Payments (Danger of Foreclosure)

The next type of don't wanter is the person who is facing foreclosure. He's behind in his payments by three to six months. This has just crept up on him little by little. Financial pressures have built up to the point where he's seeing himself being foreclosed upon. And the type of individual who lets this happen is usually a procrastinating individual who likes to hide his head in the sand and who does not really understand the serious consequences that arise out of being foreclosed upon. Once he becomes a victim of a foreclosure, his credit is virtually ruined. For a long time to come, on almost every credit application form he fills out, he has to notify the credit bureau or the credit granter that he has gone through foreclosure. This appears on his record. It is very serious, and we need to educate the people we deal with in the foreclosure sense that if we can come along and save their credit picture, we're doing them an extremely great service.

I'm thinking of one young couple who bought an investment home and couldn't make the monthly payments on it because it went vacant due to their own stupidity. So they let it go to a foreclosure situation and faced seeing an equity of $15,000 to $20,000 evaporating into thin air. Their agent approached me and said that they would be willing to exchange their $20,000 equity and the ability to have their property refinanced for almost anything that I had. They would take vacant land that they had never seen; they would take personal notes; they would take personal property. They were just desperate. "Help us out! We need help! We realize we're going to have to be flexible. We will take anything to solve this problem." And that is what happens when a person gets behind the eight ball.

7. Negative Location

The next kind of don't wanter is the person who has a property or purchases a property in an area that is declining in value, and he realizes that he has to be flexible in order just to get out and save his shirt. So this is the kind of don't wanter that perhaps we don't even want to deal with. In our analysis we have to determine whether or not it will be a long-term investment or a long-term loss.

8. Taxes

The next type of don't wanter is the person who hasn't paid his taxes, and the property is getting ready to go into a tax sale. Or it might be a person who hasn't paid his federal withholding income taxes and finds himself in April the following year having to come up with a lump sum cash payment, money that he does not have. His only hope to raise that money is by selling some property.

9. Estate Situations (Deaths)

Another type of don't wanter is associated with the estate sale. This is a special type of don't wanter. Often several people are involved. Owners of estate property are a special type people because they usually have received an investment or a piece of property they didn't expect to receive, something that they did not work for themselves. They are less emotionally attached to that property and usually are more willing to be flexible in price or terms. Now since there are a lot of attorneys handling these estate situations and

since their advice is usually to get clear out of their property, they usually give the advice to sell their property for cash. In most instances of estate sales, the prices are lower than the market prices. However, cash is necessary. I heard of one investor, a very large investor, who had as one of his rules that he would never buy a piece of property unless it was in an estate because he has learned that property that is tied up in an estate usually can be purchased at very, very reasonable prices.

10. Retirement

The next type of don't wanter is the retirement candidate. This man has worked all his life cleaning up and fixing up his particular property, and the time has come when he wants to retire. Now he's faced with several alternatives. He can sell for cash and pay enormous capital gains taxes, or he can sell for a very small down payment and have a very handsome monthly income coming in to support and sustain his retirement. This is the type of individual whom we call a don't wanter because of his flexibility. He really wants to sell his property and is willing to give good terms because of the retirement situation he finds himself in.

11. Competition with Rents and Facilities

And the next type of a don't wanter is a person who can see that his building is quickly becoming obsolete with respect to the competition that is around him. There might be new apartment buildings that have gone up around him with swimming pools and underground parking and air conditioning—things he does not have—and he soon finds that he is the brunt of all of the criticism from his tenants. One by one they slowly move out. He has to find new tenants. He has to lower the rent, and he says to himself, "I think I'd rather just get rid of this property than have to worry about putting in swimming pools and cleaning it up."

12. Out-of-Area Owners

People who live out of the area and are out of touch with the market trend frequently make good don't wanters. You and I know that if we are out of touch with our marketplace in some areas of our cities for even as short a period of time as three months, we are totally out of touch with what prices are. If an out of area owner has been out of touch with his marketplace for four or five or six months, he might be willing to sell his property at a price which we know is excellent and which he thinks is high. Management problems also increase with out-of-area ownership.

13. Neurotic Fear of Doomsday

A follower of the "Chicken Little School" of thought is anxious to liquidate all his holdings and retreat to a mountain cave. Since he thinks the crash is imminent, he'll discount his properties heavily. People who follow doomsday advice and believe real estate is going to crash are good candidates for this category.

14. Debts

There's also a very large body of people who, because of consumer debts, have found themselves having to steal or borrow from the money they would normally pay on their mortgage payments to pay off their consumer obligations. Then they find themselves getting one and two and three and four payments in arrears, almost getting themselves in a situation of being foreclosed on. And because they're under pressure, they find themselves perhaps wanting to sell for a price and terms that can solve their particular financial problem. Only recently I was discussing with a credit manager of a very large bank about his particular portfolio of mortgage loans, and he confided in me that there were in excess of 300 people served by his bank alone who were behind in their mortgage payments as much as three to six months. Such people need relief from money pressures. These types of people have gotten themselves in certain money problems that need a sale of a certain piece of real estate.

15. Ignorance of Investment Principles and Market Conditions

The next type of don't wanter is the person who does not understand the rules of the marketplace, who wants to sell at a low price but doesn't realize that his price is too low. Or maybe he wants to sell on creative terms because he doesn't understand the ins and outs of creative financing. Ignorance is a great cause of don't wanters.

16. Time Constraints

The next kind of don't wanter is the person who finds himself in a very busy occupation that leaves no time for taking care of even the minor aspects of real estate management. I'm thinking here of a busy loan officer of a bank who was promoted to a higher and busier position in his company and found he had to liquidate his real estate holdings because they took too much time away from his professional activities. I know that several of those real estate purchases were made with absolutely no money down.

17. Investment-Capital Needs

The next area of the don't wanter is the person who needs cash for other investment opportunities. This is an individual who learns about the hot tip. ACME Goldshares is going to go from $65 to $165 because of the economic situation. So he runs out and says, "Give me cash. I need it tomorrow. I'll be willing to discount my price by 20 percent. Just give me as much cash as you can. Hurry quickly! I'm going to take advantage of my other investment opportunity." This type of person realizes that he's taking a sacrifice but wants to take the sacrifice in order to get quick cash.

18. Ornery Partner(s)

Another type of don't wanter is the person who has a partner who is very hard to deal with. And so he says to himself, "In order to get myself out of a bad partnership situation, I will sacrifice my interest and sell it for a pittance just to get out from underneath it."

19. Need for Status Symbols

The next type of don't wanter is the person who wants status, who would rather be driving a fancy car and wearing fancy clothes and living the high life than owning the real estate or the property that he has accumulated. You will find this in many of the commission-type sales occupations where a person has to have a certain kind of status in order to impress his client. For this reason, many real estate sales people who have invested in real estate because they know it's good, find themselves behind the eight ball in certain respects just to make the payments on some of their status purchases. I know of one investor who caters exclusively to this type of property owner. And he has made a deal with his local Cadillac dealership that he will buy so many Cadillacs per year at $200 or $300 over cost. He drives a brand new Cadillac everywhere he goes and owns it free and clear. Every time he runs into a person who seems to think more of Cadillacs than real estate, he just walks up to him and in the negotiations he just says, "Okay, I'll tell you what. There's a nice brand new Cadillac sitting in your driveway. Here's the keys to it. All I want is the deed to your property." And that way he can discount the price of the property he is buying for a quick sale and can buy that Cadillac at a lower price.

20. Sickness

The last type of don't wanter is the person who, because of sickness or ill health, finds that the management of the property is just too much for him.

C. SUMMARY CHART OF TWENTY DON'T WANTER CONDITIONS

Key Letter	Condition	Category: Personal	Process of Management	Property	People
D	Divorce	•			
O	Obsolescence of Property			•	
N	Negative Cash Flow		•		
T	Transfer	•			
W	Wrong Management Approach		•		
A	Arrears in Payments		•		
N	Negative Location			•	
T	Taxes		•		
E	Estate Situation	•			
R	Retirement	•			
C	Competition with Rents				•
O	Out-of-Area Owners	•			
N	Neurotic Fear of Doomsday	•			
D	Debts	•			
I	Ignorance	•			
T	Time	•			
I	Investment-Capital Needs	•			
O	Ornery Partner(s)				•
N	Need for Status Symbol	•			
S	Sickness	•			
	Totals	12	4	2	2

The chart clearly indicates that the major reason for "Don't wanter-itis" is a difficulty in one's personal life.

D. HOW TO DEAL WITH THE DON'T WANTER SELLER

It's important to understand that each of these twenty don't wanter situations happens in every city to people just like you and me. It is our job to locate that don't wanter, to make sure that we negotiate with him to set a price and terms that fit within our budget. Now before we leave this subject of the reasons that make a person a don't wanter, we should understand the philosophy with which we deal with the don't wanter. I am not taking advantage of a person's misfortune. I am looking for a concentration of people who are willing to be flexible with me. It is my sincere philosophy that I am trying to solve their problem, not take advantage of their problem. And I have to solve their problem in a way that falls within my budget. I never come in to trod upon a person's misfortune and take advantage of him and then leave him in the cold.

It has been my personal philosophy that if I ever find a situation where a person wants to sell or has to sell, I always make sure that that person makes a profit on the sale of his property. And if he can make a profit and let me in on good terms, then I can make a profit. I have never had a don't wanter come back to me and say to me that he thought that I had ripped him off. On the contrar, when they bump into me on the street, they say, "Thank you, Bob. You solved my problem at a time in my life when I needed to have that problem solved. I knew that I was selling to you at a good price and on good terms. And I was willing to do that because of the problems that I was facing."

I am entering into this person's life and like a doctor, I am trying to solve

his ills and ailments by using my creative knowledge. That's my down payment; that's my power. I can solve his problem and solve mine at the same time. And we both end up in a win/win situation. It's not a win/lose situation. I win; he wins. I win because I'm able to buy that piece of property. He wins because he is able to sell that piece of property and solve his problems. That is my particular attitude, and therefore, I have to be sensitive and discrete and compassionate; I have to listen to the problem, and I have to be able to tell a person honestly if I can help solve it. And in my negotiation I even sometimes share with that person my problems so that we can get into a problem-solving mode of thinking. It's not "I'm going to buy your property and beat you down in price, and you're going to try to sell this property to me and make a killing on me" but rather "If we two get together, we can solve each other's problems, and therefore, we become friends, and we go on our merry way."

E. FINDING THE DON'T WANTER SELLER

Now that you've been able to understand some of the reasons that cause people to become don't wanters, let's go a little deeper. Let's find out where we can find these don't wanters and what tools we can use to save ourselves time in locating them.

1. The Newspaper

The newspaper is the cheapest and most readily available source of don't wanters. It is a concentration of don't wanters. Here we have people who have paid good money to advertise their property for sale. They are definitely serious. It has been said that the newspaper is just a collection of cries for help. And we are looking in the newspaper for those people who are crying for help and who are saying to us in their crying, "If you help us, we will be flexible in helping you."

a. An Exercise in Analyzing Ads. Take the three columns on the following page and circle the ones that you feel have potential for a don't wanter purchase. After you've finished that, we'll talk more about the newspaper.

b. The Art of Spotting Don't Wanters. The weekend newspaper is the best source. It generally has the largest real estate section of the week. Let's analyze what each of you will probably have to do as you finish this seminar and begin your search for investment properties. You buy the Sunday or weekend edition of the newspaper, open it to the real estate section, and begin going down each of the three relevant sections in the newspaper.

(1) "Houses for Sale" Section. You analyze the "houses for sale" section. And as you go down the houses for sale, since your time is so precious, you don't take time to call every individual ad, although that is a technique that we can perhaps use later on. You have only time to select the kinds of ads that seem to indicate flexibility on the front end. And you select the types of properties that indicate a price that is the bottom end of your pyramid of prices. Today in many of our major cities, you'd be looking for a home that is priced below $60,000 to $70,000. If you are fortunate to be located in a city that has prices even lower than that, you should be looking in the $50,000 to $60,000 range. Anything above that may be subject to a negative cash flow if you purchase it. So you should be looking between the $50,000 and $60,000 range at least at this present time. Or if you are in a high priced city, you will be looking at the bottom end of your pyramid, and you may be having to travel to another small suburb of your city to find even lower property prices.

USING THE CLASSIFIED ADS TO FIND DON'T WANTERS*

CAN YOU SPOT THE "DON'T WANTER" IN EACH OF THESE COLUMNS?

Homes For Rent/Lease

MT. WASHINGTON 2bdrm 1925 Classic. Hrdwd, frplc, tile shwr, no kitchen. City vu! Very clean. $550/mo. 213/223-7789 lv msg.

★

Clean, neat 2BR. Screened front porch. $240. Call 8:30-5 Mon-Sat, 239-9671.

Large home 4-2-2. Ar, Dr, den, wet bar, custom drapes, new,- WBFP, $650 plus dep. no pets. 298-8504.

A lovely 3br, 1½ba, dbl carport, fenced-in back yard, quiet neighborhood in NE Mesa. Phone 244-8995 between 8-5pm. By owner, lease option to buy/rent $395

4 BEDROOM HOUSE. All the extras. $675/mo. 532-4171.

Investment Properties

REDUCED So. Mar Vista 4 U. Good cond. Now $148,500. 213/839-2254 INT'L. R.E. NETWORK Staples Realtors

16-FAMILY
72XX ZEPHYR, Modern apt bldg, tenants pay own utilities, $33,600 gross. No Agents please. 469-1025.

★24U 22% DOWN
7½Xgr. Break even. $13,500 CPU Robert Deaton/Bkr. 213/995-1622

BY Owner 7 sep. 1 br units, 400sq ea. Renting for $135 ea. $2000 dn, $94,500 total. George 262-9208, 839-6354, 258-9954.

Apartment Dallas-Ft. Worth Metroplex between 66 and 300 units. Various terms available. Principals only. Clifton Jones & Assoc. 1770 West Irving Blvd Suite 6. Irving Tx. 214-259-5555.

Homes For Sale

FIRST TIME BUYER: $43,000
If you are looking for that first investment, this is your chance. Located close to beach, shopping & frwy.
Century 21 Call now 714/846-4485

Owner financed, 3-2-1, schools, no credit. Sm dn. 328-1703

FOR SALE BY OWNER
2-story colonial, 4-bedrooms, 2½ baths, 3-fireplaces, porch & pool on 1 acre For appointment call 469-3426

ASSUME MTGE.
on this 3BR stucco block home near Rome & Waters Ave. Has carport, range & ref. $30,500, $13,000 down. $204 mo. 933-7543, 932-7159-eve
BLUE CHIP REALTY REALTOR

LA CRESCENTA
OPEN HOUSE BY OWNER 12-5 PM
2 Br, new paint & carpet, prvt backyd. Upside of foothill, 3357 Stevens. $78,500 213 249-7349

STUDY THESE ADDITIONAL EXAMPLES OF "DON'T WANTER" ADS

Homes for Sale

DESPERATE OWNER!
VACANT — behind in payments. Big beautiful 3BR. 2BA. home. View of Park. MOVE IN IMMEDIATELY—No qualifying. Low down, take over total payments of $490 per mo. 10% FHA loan.
CALL TODAY • 213/962-5193
Century 21/California Gold Realty

BY OWNER
4br, 1¾ba, 1½ Eaton home. Moving must sell, lets deal. Will carry, will trade for land or cabin in or around Payson. Assumable FHA $79,500, 934-1642 or 942-5089.

2 HOMES ON ONE LOT-ALTADENA
Each 2 br., fplc. Both newly decorated $85,000. Flexible financing. Trade considered on BOTH properties.
D.J. FEENSTRA, INC.
213/798-7821 or 798-9166

NEAR METRO
3 Br, 1¾ ba redecorated, clean. Quick possession. $44,900. Owner will finance. Sunland Rlty. 242-7012.

2 DUPLEXES & 6 U's-N. of Melrose on Romaine & Kingley. $89,000-$115,000. OWC 2nd. Agt. 213/320-2222.

Investment Properties

★20 UNITS LIQUIDATION
cash flow money machine modern bldg w big upside casa motivated owner desperate for quick sale. Bkr own. will cooperate 213 395-0743

★CASH FLOW OWC LO DN
2-4-6-8 unit apts. S.F. Valley, L.A. & Long Beach. Princ. AGT. 213/851-8960

★10% DOWN
24 Two Bdrm. "bread 'n' butter" units. GA1 $59,580. Creative seller will carry loan with-low. low down. Call today for details.
DALE MARKS REALTOR 213 542-3501

30 UNITS TYLER TEXAS
Owner will finance well established Courts with Apts. & rooms plus 2 bdrm. home & 2 Comm. Bldgs. on 1½ acres on busy 4-lane street. (214) 593-1283.

★INVESTOR DREAM★
Two—Tri-plex's, 6 units, 1Bdrm, 1Ba, new, spacious, located in nice San Jacinto area. 700+ sq. ft. ea. unit. Terms. Own. must sell now! Less than 10% down.
★Liberty Real Estate 714/658-7253

Homes For Rent/Lease

BARGAIN at $425 option to purchase 3br. 2ba. lg. yard. 32nd & Shea. 264-5610.

FOR RENT or Lease Purchase. 3 or 4 bedroom brick ranch, full finished basement. $500 mo. 391-7749.

OPTION TO BUY
Family 3 bdrm $360
Don't delay call today
• • CAPITOL • • 943-5072 fee

FOR LEASE WITH OPTION 3 bedrooms, split foyer on wooded cul-de-sac, large lot. $400. 394-4913.

SAN FERNANDO VALLEY—$500—LEASE Option, NO FEE! 3 bdr. w/gst. & hobby rm, 1¾ bas. Fixer. Fenced pool. ($1500 option) RED CARPET, Rltr, 6749 Fulton at Vanowen, V.N. 213/765-8800

LEASE OPTION
Rent now and buy later. 3-4 bdrm w/wo pools, Northwest area. Call AREA CITIZENS METRO for further details. No fee. 979-5010.

OTHER KINDS OF ADS TO WATCH FOR

Mortgages & Contracts

WANTED—1st & 2nd Mtges. at discount. Fast service.
WE ALSO BUY HOUSES
Sam C. Martino, Lic Mtg Bkr
2018 E. 7th Ave. Ph 248-6111

LOOKING for mortgages at discount. Or cash, for your home. Citizens Realty, Licensed Mortgage Brokers. 4601 W. Kennedy Blvd. 879-2009.

•CASH FOR SMALL—2nd—TD's NO FEE—MALTZ REALTY CO. •213/550-1266

★I BUY TRUST DEEDS
Super fast, best price, any area
MR. SIEGEL 213/386-3445

Cash For Homes

145 REAL ESTATE WANTED

FAST CASH FOR YOUR EQUITY!

Call us for quick action. We can usually rest your mind within 8 hours. For appointment call Carrollwood 962-1579 or Interbay-Palma Cela 251-5481.
REALTY WORLD
Bobler & Associates
Realtor

Ads with "Hitches"

O DN NO PMT 45 DAYS for qual vet. Some with no closing costs. Call AREA CITIZENS METRO 979-5010.

OWNER ANXIOUS
Splendid 3 bdrm. w/pool & spa in nice neighborhood. Seller has moved & MUST SELL now!!
Sterpa Realty Register 213/368-9511

$150 DOWN
Plus closing cost on this 3-1-1 brick starter home. Ch/a, carpet, built ins, $28,950. nites 279-8010.
Century 21 Beezley 270-7487

*These samples were taken from *The Arizona Republic, Dallas Times Herald, Los Angeles Times, St. Louis Post-Dispatch,* and *Tampa Tribune.*

Each ad that indicates flexibility is circled. You have to be aware of real estate companies who advertise the flexible type advertising such as "owner anxious," "owner transferred," "5 percent down payment," and "no down payment." Many times these are just come-ons to get you to call, and you have to be aware of them. In most ads indicating "no down payment" or "5 percent down payment," they are advertising for an owner-occupant. They are advertising for someone to buy that house and live in it and therefore go through the standard government financing (F.H.A. and V.A. in the United States, C.M.H.C. in Canada). Since most of us have already purchased our own homes, we're not going to be able to use such financing legally, so we are not going to be interested in calling on that type of property. We might circle in a period of half an hour or 45 minutes perhaps 10 or 15 ads.

(2) "Houses for Lease" Section. The next column in the newspaper that we read is the houses for lease section. In the houses for lease section, we have certain kinds of don't wanters. Two specific types of individuals are advertising here.

The Investor Type

The first type is an investor who has purchased the house in question and who is renting it out and hoping to attract a tenant to make the mortgage payments for him. And in most instances the investors are not going to be a great source of don't wanters because they are trying to do the same thing we're trying to do.

The Novice Type

The second type of individual who is advertising in the "houses for lease" section is the individual who's gone out and purchased his second home. He is now making payments on both houses and can't afford it. So he says, "Well, rather than sell my house, I'll just rent it out and make my mortgage payments and worry about selling it later." He really is not an investor. He doesn't want to rent his house out. He doesn't know anything about management, and he would be more than happy to sell it, and that's why he's advertising. But he can't sell, or doesn't think he can, so he's advertising it for lease in order to save the payments.

This last type of individual is more of a don't wanter than the first type, and there's a technique discussed later on in the seminar called the "lease with option to purchase" that is just perfect for this type of real estate don't wanter.

With respect to the first type of don't wanter, you're going to find certain individuals who have advertised their property for rent and who are investors. But because of their unsophistication, they have written a very poor ad and don't get very many people calling on it. After two or three or four week's time, they find that they still haven't rented their houses out. They've had to make their first payment, and they start to have second thoughts about whether it's a good idea to rent houses out.

Tips on Spotting Ads

You'll notice that there are several kinds of ads in your paper. One will say nice fancy home with fancy this and fancy that with a lot of adjectives. Because it is very well written, it will attract your attention. Well, these types of ads will draw many, many people. On the other hand, the small little ad that doesn't tell you the location and doesn't tell you the rent and doesn't reveal any of the amenities of the property does not get very many calls. Many people don't know how to write a proper ad. Sooner or later, therefore, they may find themselves in financial trouble or become don't wanters for the property they bought. Because they don't know how to rent it out, they think it can't be done and that it's impossible. So they really get soured on their investment. It's good to give those types of people a call and ask if they are willing to sell because a certain percentage of them are going to be flexible.

(3) "Apartments and Income Properties" Section. The next area of a newspaper to inspect is the "apartment/income (or revenue) property" section. And here I'm going to locate all of the types of properties that are being rented out as apartment buildings. Once again I'm going to be looking for certain kinds of clues. I'm going to be looking for the person who has an excellent price or has an excellent location or who is advertising certain flexibilities. Of particular interest are phrases such as: "will carry the contract," "owner will finance," "owner will carry the paper," "owner will exchange," "come one come all," "make an offer," "owner flexible." These are the kinds of ads that we're going to circle and call on.

Once I have done my day's work with my weekend newspaper, I might have circled 30 or 40 ads. And I'm going to call all these people. My approach is going to be to find out as much information as I possibly can. We're going to be discussing the seller analysis here in another few minutes. The exact types of questions that will be asked will be discussed later on in Section F.

c. Gathering Information on the Phone. Each ad that you circled must be called. Take notes on every single one of them. Some of my students use three-by-five cards and cut out the ad and paste it on the corner of such cards. Others keep copies of every paper and make their notes beside the ad with a felt-tip pen. Do whichever way seems to fit your particular style. I find if I spend too much time cutting out the ads and pasting them on three-by-five cards, I spend more time pasting than I spend looking. What's important is to find that piece of property, not worry too much about being neat about it.

d. Beating the Competition to the Punch. You will understand that there are some people who take this so seriously, who understand that there is such a small percentage of really seriously flexible people in the marketplace, that they will go to the newspaper or a newspaper agency in the wee hours of the morning and pick up the newspaper as it comes right off the press. This enables them to be the first people to call that particular don't wanter. There is an adage that we need to use in our business more often, and that is, "You don't steal in slow motion." Translated into win/win language, this means that the bargains don't last long. When a seller calls out for help, you had better be prepared to strike a win/win deal in a hurry. When you find something that's hot, you need to act on it quickly. So when you're dealing with the newspaper, you call everyone you have circled and try to find the people who are flexible. Then you pursue the analysis deeper so that you can get to an offer.

If you don't happen to find anybody in your newspaper for that Sunday to call on, just wait until next Sunday and start the process all over again. We have to be like "nothing down investors." We have to be patient. It may take us one week to find our first investment, or it may take us 25 weeks. Sooner or later we will find it.

e. The Shotgun Approach. Now if you really are a very impatient type person, too impatient to use the rifle approach (that is, zeroing in on the people who are advertising their flexibility), you can use instead what I call the shotgun approach. Let me tell you an example of a particular Florida investment group consisting of four or five members. Once a month they get together on a Friday or Saturday evening at the office of one of the members where there are several phones located. Each of them takes a different section of the newspaper, in the classified section, and each person calls every single ad in his section. What they have is four or five different people calling every single ad that is advertised. They call real estate companies; they call "for

sale by owners." And they have one simple line that they use on the phone, and that is, "Mr. and Mrs. Seller, Mr. and Mrs. Real Estate Agent, I'm an investor, and I'm going to buy one house tonight. I'm going to buy it from someone who is going to be extremely flexible in either price or terms. This property will be closed in 24 hours or 48 hours or in as short a time as possible. Are you interested? Are you interested in selling on short notice with excellent price or terms?" Something of that nature. Most of the people when they call are not interested, but a small number of them are. In a newspaper of the size of your city, you might find four or five, not a large number. Each of those people, according to this Florida investment group, is talked to, called. They visit the property; they inspect it; they go back to their dinner appointment; they eat; they talk; they analyze; they decide on the one they want. Then they go back to that person and buy that property before the evening is out. And they put the property in their portfolio and wait until next month to buy another one. Their goal is that they are going to buy one house each time, and that's the way they do it.

f. Running Your Own Ad. Now, the next concentration of don't wanters can be located by running your own ad in the newspaper. There are two kinds of ads you can run. You can run the shotgun ad, or you can run the rifle ad.

(1) The Shotgun Ad. The shotgun ad reads something like this:

> Cash for your equity in 24 hours.
> Call Bob, 828-3737.

You are going to attract a certain type of individual here, one who has tried to sell his property before and has not been able to sell it, one who realizes that anyone who advertises that kind of ad in the paper is usually going to require a substantial reduction in price. But this is the type of individual who's been through it all, who's tried, who hasn't been able to

Now there is a special section in your paper called "real estate wanted." This is where you run these types of ads. Why do you see this column consistently being used in the newspaper? Why do people continue to spend their good money advertising in columns like this? Because it works. Because they realize that they may have to spend $200 or $300 a month advertising with an ad like this every day or every Sunday, but that it only takes one person, one property purchase to recoup the entire advertising investment for an entire year's time.

(2) The Rifle Ad. The next kind of ad is a little more explicit. It is the rifle ad. It reads something like this:

> I buy real estate from distressed sellers. Will give you a high price if you are willing to sell on easy terms. Can close in 48 hours. No closing costs. Bob, 828-3737.

Not very many people are going to respond to this type of ad. It narrows down all the curiosity seekers. I know one woman investor who runs an ad like that. It is even a little more explicit than the one shown, and she says that not very many people call. However, when they call, she knows that she has just bought a piece of property if she wants it. She might only get two calls in a three-month period of time. But she'll buy one of those pieces of properties, and it's been well worth her money. She's very busy and doesn't have the time to do a lot of her own looking, so she lets people look for her.

2. Real Estate Signs

People advertise their property for sale by putting a sign on it. Real estate companies put their signs on property and so do owners selling on their own. If you want to take advantage of these leads, stop at every real estate property

that has a sign on it and talk to the people. You're going to locate a person sooner or later who is willing to be flexible in price and terms. It just takes a great deal of time and effort. And you can find that your time is much better spent by looking in the newspaper or using some of the other methods we are going to introduce.

a. Checking the Market Pulse. Still, there is value in following up on signs. For example, it is a good way to check out the market pulse to find out what properties are really selling for in that specific neighborhood. If I spend a good solid hour in one particular neighborhood, by stopping to check with all the people who are advertising their properties for sale, I will be able to know within a few thousand dollars what property should be selling for in that neighborhood.

b. Practice in Negotiating. It is an excellent education and also an excellent opportunity for the beginning investor to have a practice run at negotiating. It is an excellent opportunity to try out your techniques on somebody, to see how hard it is to ask somebody to sell their property with little or no down payment. It is a good way to get all the bugs out of the way when you talk with people. It is a good way to become familiar with the lingo. And so I recommend that you stop at people's property, and you ask them what they are selling for, just to find out what the market pulse is.

3. "Buying Farms"

Don't be confused by the term "buying farms." This doesn't mean that you go out and you buy farms. It just means that you pick a certain area of your city, and in that particular area of your city, you contact every single owner by letter or in person, and you ask them if they are interested in selling their real estate. You are going to find that there are a certain number of people who are willing to sell their real estate, and there is going to be a very small percentage of those who are willing to sell with excellent price and excellent terms.

I started out this way. I made an elaborate map of a 10-square-block area in my city, which I thought was an excellent location, and started by contacting every single owner of property around every single block. And after getting around two or three blocks, I found a fellow who was a don't wanter. I bought his property from him using the second mortgage crank technique, which we will be discussing later on. I was able to buy it with little or no down payment, and that property purchase led me to another property purchase, which led me to another property purchase, and I have never gone back to my elaborate map since. It was a way to get myself started.

4. The Courthouse

The next area of concentration of don't wanters is at the Courthouse. In the U.S. we speak of the "County Courthouse"; in Canada the "Provincial Courthouse" is the term used. Each of you should become familiar with how the courthouse operates and what kinds of information are recorded there. I would highly recommend that you go down to the courthouse and spend an afternoon walking through the offices, such as those of the County Recorder and the County Clerk (in Canada, the Land Titles Office). Check with the bulletin board on estate sales, foreclosure sales, tax sales, bankruptcy sales, and ask those who are informed how these items are recorded in your particular city. It would be wise for you to go to your County Recorder's office (or Land Titles Office) and give the person in charge the address of the property where you are now living, whether you own it or not. And ask him to help you locate this address in the records so that you can get a feeling for how this information is recorded.

I have taken the opportunity to go with a title officer who took the time

when he was working at the courthouse, to show me some of the little secret ins and outs of how the system works. He showed me how a person can get vast amounts of information quickly and without a lot of red tape. In the courthouse (or Land Titles Office) there may be seven or eight different concentrations of don't wanter owners which may prove to be very profitable. (Certain information may also be available through the office of the planning department, and in Canada at the office of the city assessor.)

a. Estate Sales. For example, estate sale notices are available at the courthouse. These are also advertised normally in the local newspaper under "Public Notices." And they are also found in a publication that I will refer to later on. The trustee for every estate, usually an attorney, advertises in the courthouse to locate people who might be interested in buying the property. As we mentioned earlier, people who are interested in the estate are a little less picky about their price than ordinary people because they find themselves in a situation where they would like to cash their equity out. They would like to be able to go their own separate way.

b. Foreclosure Sales. Also available in your courthouse is certain information about properties to be sold in a foreclosure situation. These are properties that have been delinquent in their monthly payments, and the bank has filed a foreclosure notice that the property will be sold on approximately the date indicated. In many instances in the United States the sale occurs on the courthouse steps. The process that is involved is that the person who has filed a default has called for the property to be sold to satisfy a certain obligation.

Suppose you have a $50,000 house, with a $37,000 mortgage which is in default. The holder of the mortgage files a foreclosure notice. The property then goes to a foreclosure sale; and if remedy has not been made before this sale, it may be sold to the highest bidder. The person who holds the underlying $37,000 first mortgage is, of course, there to make sure that the highest bid is at least $1 higher than the amount of the mortgage money due. That way they can pay a dollar fee and repossess the property. Then they will put it back on the market for a normal sale to satisfy the obligations of a $37,000 mortgage. In American practice, anyone else who comes to that foreclosure sale and bids for the property—suppose he bids $38,000—has to have a cashier's check for that amount and be prepared to pay that amount immediately. One of the detriments of the foreclosure process, therefore, is that large, immediate payments are often required. However, if a person has done his homework and checks out the value of the property and can provide a bid with the right amount of cash, he can make substantial amounts of money. One of my friends recently purchased a house on a foreclosure situation that was listed at $120,000, and he was able to buy it at $80,000 on a foreclosure sale. This is not at all unusual. Large profits can be made by investors who understand the foreclosure process.

The process of finding out about such information is to go to the public record. Those investors who are experts on foreclosure properties have to do a great deal of undercover work, determining out who the owner of the property is and what his particular problem is. Perhaps they contact him and make an arrangement before the sale takes place. Many foreclosure problems are resolved long before the property is actually sold. It is my personal opinion that we will be seeing more and more foreclosure sales coming in the near future, especially in times of economic belt-tightening. People are getting more and more into consumer debt and becoming more and more purchasing-oriented. We will find people getting themselves behind in their payments and getting themselves in trouble. Inflation and

high interest rates are the direct cause of this kind of problem. In the future, foreclosure sales may be an extremely good area of investment.

I know that one of my graduates who concentrated in this area bought, with a partner, a 12-unit apartment, a four-plex, and 10 houses in a short period of time, all through the foreclosure process.

c. Tax Sales. The next area is tax sales. This is a public notice item also. These properties are being sold to satisfy the demands of the local jurisdiction for the property tax that is due. Sometimes tracts of land have been six, seven, or eight years without having their taxes paid because either the owner is dead, or the heirs have forgotten, or the property has just been abandoned. So the appropriate office has put them up for sale on the open market to pay the taxes. And usually the properties can be picked up for cents on the dollar.

d. Bankruptcy. Bankruptcy sales are also a matter of public information. These have to do with individuals who file for bankruptcy or people who have had their assets seized in a bankruptcy situation. And these assets are sold to satisfy the demands of the creditors.

e. Suits and Liens Filed. As a matter of public record, you can find all of the lawsuits that have been filed against individuals in your local jurisdiction. With a little bit of research in the appropriate office, going through all the suits that are pending, you may find people who are in a bit of financial difficulty.

f. Divorces. In addition to these suits, you may find people who are filing for divorce. These are particularly interesting sources of don't wanter owners. For our American students: if you go to the County Clerk's office, you will notice that the lawsuits that are filed are kept in legal-size folders as a matter of public record, and anyone can look at these files. If you go and ask your County Clerk to let you examine the past three or four months of legal files, you will notice that many of these files will go into divorce proceedings. As you know, a large percentage of these people who go through divorce will be interested in selling their property sooner or later. By contacting them before they make their final decision, you might be there at a time when they are more flexible in the disposition of their property.

For our Canadian students: in Canada, divorce information may be more difficult to acquire. Where a number of papers used to publish divorce applications and decrees, this practice has generally been curtailed in view of "invasion of privacy" concerns. Still, where possible, make the attempt to obtain divorce information, which is potentially very helpful in the search for don't wanter properties.

One way to approach these people is to locate all the divorced couples who own real estate and send them a standard form letter, which states in a very sensitive way: "Mr. and Mrs. _____, we understand that because of circumstances in your life you may be interested in selling your real estate. We would be more than happy to make an offer if you are interested. If you are interested, please contact _____." This is one way of locating people who may be interested in selling their real estate.

g. Out-of-Area Owners. It is also possible to use the county courthouse to find out the address of people who are out-of-area property owners. It is important to find out where the tax notices are being sent. If the tax notice is being sent out of the area, it is a good chance that the owner is an out-of-area owner, and he may be more willing to sell. He might have distance problems with the ownership of this property. And he might not understand the value

of this property, and you could make him an offer and entice him to sell.

One of my recent graduates, who was a law student and did not have a lot of money, spent several hours in his county courthouse and located the names of 33 out-of-area owners of income property. And he sent out 33 letters and in the course of a few weeks received back eight replies. Six of these replies were negative, and two were interested in selling. One of them was an extreme don't wanter who said that her three-unit apartment building was causing her ulcers and all sorts of problems! She said that she just wanted to sell and would he be kind enough to take the property off her hands. Of course, he was able to negotiate the purchase with absolutely no down payment.

5. Commercial Record

The process of using the county courthouse files (in Canada the municipal and provincial systems) for obtaining information is an important one. It is so important that this information is available in your particular area. In regard to these commercial records, commercial publishing companies just go down to the county courthouse and do the same kind of work that I am suggesting that you do. This publication in our area is called Intermountain Commercial Record. In other areas the name varies, but you can usually obtain a copy of this record by going down to your public library, or to a prominent title company in your area, or to the Land Titles Office (Canada), or to an attorney who handles courthouse and legal proceedings. At any rate, this publication is much like a commercial newspaper, except that the advertisements in them are for bankruptcy sales, tax sales, foreclosure sales, and estate sales. Listed there also are all the people who have filed for divorce throughout the period covered by the publication. And all the people who have lawsuits and liens filed against them, and the people who have just taken out new mortgages will be listed. In some cases, the births and the deaths in that certain period of publication are given, as well as lots of other information.

6. Attorneys

Attorneys who handle divorces and estate proceedings would be an excellent source of don't wanters. I make it a habit always of asking the attorneys with whom I am dealing, or my friends who are attorneys, if they might be interested in referring me to their clients who might be interested in selling their properties.

7. Accountants

The same thing goes for accountants. Usually when a person has a tax problem, he will talk to his accountant first about the disposition of his property. You can obtain a very good lead that way.

8. Bankers

Bankers and other lending officers are the first persons to know that a person is behind in his payments. And each bank (or Credit Union or other lending institution) has a person who is assigned to call up those individuals who are behind in their payments and "harass" them until they make their payment. It would be useful to locate that individual at your lending institution or bank and have him mention to those people he calls that there is an investor who is interested in buying some property, and if they are interested in selling, he would give them the card of this investor. That would be an extremely good source of don't wanter owners.

Each one of you might find that it is interesting to establish contacts with lending institutions, credit unions, etc., and let them know that you are interested in buying properties, and if they have anybody who is extremely anxious to sell, you might be able to help solve that problem.

Lending institutions do not want to foreclose on those properties. They may be mandated by law to hold only a certain percentage of their assets in

real property. The only thing they want is that the mortgage payments be made current; if you make them, fine; if someone else makes them, fine.

9. Friends and Acquaintances

Of course, friends and acquaintances should always be notified that you are interested in property and that if they find a piece of property for sale, and the owner may be flexible, to give you a call.

10. The Finder's Fee Method

The next method is the finder's fee method. You might go even so far as to offer the finder of the property a small finder's fee. If there is a piece of property on the market that you buy, you might give the finder of this property $200 to $300.

During one summer when I was very busy, I did not have time to do concentrated searching for don't wanter owners. I had hired a university student during the summertime, and he spent full time looking for real estate for me, calling all the ads in the newspaper and going to the local universities and getting a list of all the owners of property, calling them and sending them letters, and talking to local real estate agents, looking in the multiple listing book, etc. And I paid him a certain fee for every property he found for me that I bought. During that summer, using his efforts, we were able to locate three or four excellent pieces of property that were being sold by don't wanters, and we were able to make some profits through the use of a finder's fee method. Each state or province has different laws with respect to this method. And you might want to check with your local laws to see if it is possible for you to pay a finder's fee to someone without violating prevailing procedures and legislation.

11. The Real Estate Agent

The last and most important source of don't wanters is the real estate agent.

a. The Real Estate Agent as Investor and Don't Wanter. We have two categories here; the first category is the real estate agent as an investor. In many circumstances the agent finds himself in a situation where he has first crack at all the well-priced properties on the market. The smart agent learns quickly how to pick up these profits for himself. I have been able to observe, at least in my area, that whenever I go into a real estate office and mention that I am looking for some property to buy, several agents in the office own personal properties that they might be planning to sell. The main problem with being a real estate agent is that the income is spotty; it comes in chunks. And many times the chunk that comes in is already spent before it is received. So many of them are living a hand-to-mouth existence. Those of them who do own real estate find themselves in a situation where they have to sell their real estate because their income did not come in as expected. So the real estate agent himself is an excellent source for don't wanters.

As we will learn later on, there is a society of exchange counselors who are real estate agents and represent clients in the purchase, sale, and exchange of their investment properties. The words "don't wanter" originated from exchanging jargon. A don't wanter in the exchange world is someone who wants to get rid of his property in exchange for another piece of real estate. In many instances those exchange counselors who are involved in the exchange business—exchange real estate brokerage—have picked up these don't wanter properties from their clients and can put them back on the marketplace for eventual sale. This is an excellent source of don't wanters. We will learn later on about exchange meetings and how to take advantage of locating don't wanters in these exchange rings.

b. The Real Estate Agent as Finder. The second way to use a real estate agent is to have him be the finder for you. In my mind, the primary function of a

real estate agent is to locate investment opportunities for you, his client.

(1) Advantages. There are many advantages of using a knowledgeable real estate agent. He has all the referrals to banks and lending institutions; he has been through this process time and time again and understands it implicitly. If you are just getting started, he is an excellent source of help. He has experience and expertise; he can do appraisals. His appraisals save you hours of checking and usually don't cost you anything. He is also able to locate bargains and is able to get a first crack at the multiple listing service on properties or new office listings.

(2) Disadvantages. There are disadvantages. The job of real estate agents is to feed their families and to make enough money to keep himself or herself alive and healthy. Therefore, they are tuned toward their own money interests. They have to make a sale, or they don't eat. They are less likely to deal with a weak investor. They really only want to deal with those investors on both sides who have properties for sale or have the advantages to buy. Since they are in this business to make a living, they will in the long run represent themselves. They are also obligated to have complete allegiance to the person from whom they collect the commission. And this is generally, in most areas of the country, the seller. The seller lists the property and pays a commission when it is sold. Therefore, the real estate agent will be on the side of the seller. Note: the legal and ethical obligations of the licensed real estate agent are often clearly expressed in the format of standard forms used in the transactions. Still, many times agents may keep back the information that is necessary for us as the buyers to know. I say this not in a derogatory sense. We would do the same thing if we were in their shoes. They are, therefore, resistant to creative transactions with nothing down motivations, because if there is no money involved, there is no commission involved. To make that kind of offer to the seller not only goes against the interest of the seller, but it goes against the agent's own interests. And so agents are going to be the ones most adamantly opposed. They don't really think that that kind of an offer is possible, and they don't want it to take place, because it works against them. However, the advantages outweigh the disadvantages. A good real estate agent is worth his weight in gold. If you work exclusively with agents, you will find that the good agents are conscientious and work hard for you. They will find you excellent pieces of property. In summary:

The Advantages of Using a Real Estate Agent:

1. Referrals to banks and lending institutions
2. Expertise and experience
3. Appraisals of estimates of value
4. Locates bargains—first crack at the MLS or office listings

The Disadvantages of Using a Real Estate Agent:

1. Tuned in to own money interests
2. Obligated to seller (unless you employ a buyer's agent)
3. Resistant to creative transactions in many cases

c. Six Rules for Dealing with Agents. I have found that there are six specific rules that I use in dealing with agents to find new properties.

(1) Give Them Specific Guidelines. First of all, I give them specific guidelines so that they are never left in the dark about the kinds of property that I am really interested in buying. I give them the symptoms of the don't wanter, the kinds of things that the don't wanters might accept.

Ten Percent Down or Less

For example, I'll say to a real estate agent, "If you could ever find an individual who is willing to sell his property with a 10 percent down payment or less, give me a call immediately." I know that if I can find someone who is

willing to sell for less than 10 percent down, I can normally structure it as a nothing down transaction as far as I am concerned. I am not referring here to a 10 percent down payment and a refinance. I am referring to a contract sale with 10 percent down.

Fifteen to Twenty Percent Below Market

The second guideline is to find a seller who is extremely strapped for money and is willing to discount his price to 15 or 20 percent below the market price for quick cash amounts. I am very interested in looking at such a property, and if it is an attractive investment, I will raise the funds if necessary to buy it and put it in my portfolio. Therefore, I am very open to that kind of offer. We will show you later how to raise the cash.

Twenty-five Percent Second Mortgage Carried Back

I also tell my agent that if he is ever able to find a seller who has a lot of equity in his property and who does not need all that equity in cash but who might be willing to carry back as much as 25 percent of the total purchase price of the property in the form of a second mortgage, then I am extremely interested. More on this technique in Section O.

Those are the three guidelines—10 percent or less down, 20 percent below the market price all cash, 25 percent on a second mortgage. Any one of those three guidelines or criteria can lead me into "Nothing Down" transactions. Therefore, I am very interested in having my agents bring me those kinds of properties. Normally, an agent who hears those kinds of guidelines says to himself, "Yes, I've heard this before. Who isn't looking for that kind of property?" And they might discount your wishes as those of a crank investor. Those of us who have been in real estate know that there are a lot of cranks out there who would have you spend your time spinning your wheels looking for investment property and then never buy anything. We must convince our agent that we are desperately sincere about these kinds of criteria given them.

(2) Try to Locate at Least One Good Real Estate Agent. I have found it in my best interest to go to several real estate offices and talk with at least 20 or 30 real estate agents about my particular wishes. And those agents who are sincerely interested in working with me soon begin calling me with properties to purchase. An alternative is to hire the best agent or broker you can find and hire him (or her) to represent you (not the seller) in locating properties (buyer's broker arrangement). See page J-6 for details.

(3) Immediate Inspection. And in order to make sure that I get at least one very willing and eager and conscientious agent really working for me, I instigate an immediate inspection of the property so that he knows that I am not giving him the run around. I explain to him that it is not necessary for him to pick me up in his car and drive me over to the property, that I am more than capable of driving my own car and inspecting the neighborhood, which is an important aspect of the investment anyway. If I like the neighborhood and if I like the outside of the property, then I can call up the agent and have him arrange a meeting with the seller at the property to do an interior inspection. If I don't like the outside of the property, then I am not even interested in meeting with the seller.

I try to let the agent understand that I'm trying to save him time and myself time by not getting together with him and having him show the property. As soon as the agent realizes that this is in his best interest and you are just trying to save time for both of you, he will be more apt to help you.

(4) Fact-find with the Seller Yourself. The next step is to try to have a discussion with the seller. Basically the topic is his property. This may not be a negotiation session but rather a fact-finding session, a session where I ask the seller for the specific information that will help me determine how I will make an offer. The agent may be present at this meeting, but you should try

to get the agent to understand that it is not his role to interfere in this particular fact-finding session, that you do not want him to go and ask the seller this information for you, but that you will do it yourself. The reason that you do this is because the specific questions that you need to ask are very sensitive and need to be done very carefully. Once you have been able to visit with the seller and do an interior inspection of the property, then you can proceed to have the agent carry back and forth the offer between you. But it's extremely important to visit with the seller face to face first or at least have a conversation on the telephone.

(5) Borrowing the Agent's Commissions. The next step is to establish a relationship with the real estate agent whereby after several transactions have gone by, he will be willing to lend you his commission if necessary to complete the transaction. Now this does not mean that you are taking advantage of your agent. I don't mean to put it that way. The agents benefit from this because they can receive a steady monthly cash flow to offset the ups and downs of their income schedules, and they are making money sooner or later from these commissions. I don't want to indiscriminately borrow money from my agents; I only borrow it when it's necessary and when I don't have the other funds to complete the transaction. It is, of course, subject to negotiations.

(6) Using the Multiple Listing Book. Your real estate agent can help you in finding don't wanters by using the multiple listing book. The multiple listing book is an obvious source of don't wanters, isn't it? These are people who have gone so far as to list their property with an agent. Many of these people are really more flexible than the agents think or know. In most cases the sellers don't share with their agents the reasons why they need to sell their property. And that is one of the biggest reasons why we have to visit with the seller personally. The multiple listing sales book technique that I am going to describe now shows you how you can use your multiple listing sales book to locate don't wanters.

A Case History

According to a true account, a fellow from a California city who was a commercial investment broker listed a piece of commercial property and sold it in a 30-day period of time and collected a 10 percent commission of $100,000. He had stopped with his friends in the bar, and one of his friends was a residential salesperson who sold houses for a living, an agent. The residential salesperson said, "There's no way in the world that you could sell $1 million worth of houses in a 30-day period of time like you just sold $1 million worth of commercial property." And this broker, being just a little bit drunk, replied, "I'll bet you $10,000 that I can sell $1 million worth of houses in one 30-day period of time." And so they bet on it, and the bartender witnessed it. The next morning as he wakes up with a little bit of a hangover, he vaguely remembers the bet he made, and so he goes out and starts to look for buyers to sell $1 million worth of houses to. He starts out, but the first two or three days he doesn't do too well. And as you residential real estate agents know, it's not too easy to sell $1 million worth of houses in a short period like that, so he was discouraged, and he said, "Well, I guess I'll have to resort to creative thinking. My bet was that I would be able to sell $1 million worth of houses. Who should I sell these million dollars' worth of houses to? Could I sell those million dollars' worth of houses to myself?" And so he said, "Why don't I see if I can't buy the million dollars' worth of houses in one 27-day period of time." So for the next 27 days he took a group of high school girls or college girls, and he sat at his office with the current multiple listing books and took the right kinds of properties right out of the multiple listing books and wrote an offer on every single property that fell within certain parameters and wrote every offer at 20 percent below the market all cash, to be closed in a certain period of time and sent the girls out with the offers. He'd write one

offer, give it to a girl; she'd go out and present it. He'd write up another offer immediately and give it to the next one, and she would go present it; then he would write another offer right there on the spot and she'd go present it. This went on for 30 days approximately. During that period of time he wrote 1,750 offers, and some 40 of those were accepted for just over $1 million worth of real estate. Those houses were all 20 percent below the market. Now he hadn't closed on those houses yet. He had $100,000 cash in his bank account that could help with the down payment; he also could use his commission as down payment; he also could use the $10,000 bet from his friend as part of the down payment, and if he was short any, all he had to do was to go down and find some partners, some doctors or some dentists, who would like to participate in a very lucrative investment.

To my understanding, this person is not a broker anymore because he spends his time investing in the real estate market. He learned how to use the multiple listing book, and by making offers on every property, he was able to find out which ones were flexible and which ones were not.

Now one last comment on real estate agents: let me say that they can be your best friend. They should be used, but you should learn how to find the agents that are going to work for you. By following the specific rules we have outlined in dealing with real estate agents, you should be able to find don't wanters over a consistent period of time.

FINDING AND DEALING WITH DON'T WANTER SELLERS

By Robert G. Allen

Use this chart to identify don't wanters, analyze their needs, and plan your negotiation strategy.

TYPES OF DON'T WANTERS	PROBLEMS OR CIRCUMSTANCES	PROBABLE SOURCES OF THIS KIND DON'T WANTER								CLUES AND KEY WORDS TO LOOK FOR	KEY MOTIVATORS: PLACE EMPHASIS IN NEGOTIATIONS
		Newspapers	MLS Book	Real Estate Agents	Courthouse	Property rental cos.	Exchangors	Drive around looking at properties	Successful investors		
DON'T CARE ABOUT CASH	1. Management problems	●		●			●	●		mgt. problems, negative cash flow, high loan/low equity	1. Stress quick closings so that seller can rid himself of problems quickly. "We could arrange to have this problem out of your hair in 24 hours."
	2. Transfer/out of state.	●		●	●	●				transfer, out of state, moving, date for move is very close	2. Stress quick closings plus saving commissions if property does not sell fast. Seller won't have to leave wife and list with real estate agent. He can use your note as down to buy house in new city. "You don't need any more stress at a time like this!"
	3. Behind in payments.				●					behind in payments, motivated seller	3. Stress credit rating and how important it is to save it. Stress ability to pay back payments but that is all. (You can get the money from a partner later, if you're worried about the money.)
	4. Fixer-upper.	●		●			●	●	●	fixer-upper, handy-man special, needs work, property not rented out because it needs work	4. Stress his problem property and how nice it will be when he has the headache out of his hair. "Life is too short to worry about this."
	5. Time problems, too busy.	●		●			●		●	other interests — going on long vacation, promotion to new job	5. Stress quick closings. Stress importance of time and how precious it is . . . how it's not worth wasting on something you can't stand.
	6. Sickness/ health.	●		●			●			Too much for me to handle, seller in hospital, other family members handling investment.	6. Stress quick closing. Stress cash flow to help with medical bills.
DON'T NEED CASH	7. Divorce.	●		●	●					Single owner, divorce	7. Stress starting a new life . . . how important it is to cut your losses and run with your winners. Stress psychological freedom that will come when this "curse" is removed from your neck.
	8. Retirees.	●		●			●			Time to relax, retirement near, needs cash flow to supplement pension.	8. Stress cash flow to aid retirement and tax savings for no down payment sales. "Why pay all that money to the government when you could use it for a better retirement."
	9. Already bought new property.	●		●		●				Option to buy, buy or rent, rent to own, vacant	9. Stress how he doesn't need any cash. Your payments will coincide with his so that he is not at a disadvantage. Offer to pay the same interest rate he has on his new loan . . . or higher.
	10. Investor, builder.	●	●	●		●	●		●	Interest in % return, will consider trade, need to sell out subdivision to clear bank loans, slow moving projects	10. Stress the amount Uncle Sam will take of his profits if he gets cash. Offer to pay him more than he would earn at the highest local "paper" certificate return. Stress security. Remember "greed."
	11. Wealthy owners.			●		●	●		●	Don't need cash	11. Stress no necessity of cash. Stress profit. Stress that you are an honest, hard working individual who is trustworthy but cash poor. "How did you get your first break?" Act like a beginner, let him "counsel you." Try sympathy.
DON'T WANT CASH	12. Tax problems.	●	●	●			●			Installment sale; low down; exchange only.	12. Stress tax consequences — the best way to avoid this is to sell with little or no money down. Offer to bend over backwards to help him with his tax planning.
NEED SOME CASH BUT NOT ALL	13. Flexible seller.	●	●	●			●			Will carry second, paper, OWC, wrap around mortgage, owner will finance, consider second, contract sale, no qualifying, low loan/high equity, seller doesn't need to have his money for several months, even longer but wants to sell now, needs cash for small consumer items that could be obtained with a credit card (not ours). Debts to be paid off.	13. Stress the ability to get him the cash he needs for his minor problems but that it will be necessary to carry some paper. Stress honesty and ability to close. Credibility is all important.

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SECTION F

Seller Analysis

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Seller Analysis

F

A. THREE MAJOR OBJECTIVES OF THE INITIAL CONTACT ..... F- 3
B. SETTING THE STAGE ..... F- 3
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Seller Analysis

F

The most critical factor to look for in analyzing the seller and his situation is *flexibility*—how willing the seller is to accept creative terms. If the seller is a flexible don't wanter to begin with, the buyer's task is 90 percent completed. The rest is a matter of win/win problem solving.

In general, there are two broad phases of interaction between the buyer and the seller. The first is the initial "sounding out" contact. The second is the more detailed negotiation related to the formal offer to purchase.

A. THREE MAJOR OBJECTIVES OF THE INITIAL CONTACT

The three major objectives of the initial contact with the seller (whether by phone or in person) are:

1. To assemble and interpret clues that will indicate the flexibility of the seller (a direct function of how much of a don't wanter he is);

2. To gather significant information about the property and how it might eventually be financed; and finally,

3. To build up trust with the seller so that he will have confidence in you.

Since the buyer-seller interaction is the most important scene in the investment "drama," it is critical that the buyer be clear about his or her role.

B. SETTING THE STAGE

The attitudes, assumptions, and objectives of the buyer *vis-à-vis* the seller—i.e., his role—need to be clear prior to the interview. Naturally each buyer will proceed from a slightly different frame of reference; however, the following five points will begin to outline a pattern that has proven very successful over the years:

1. People First

Of course, your primary objective is to obtain solid investment properties with little or no money down from your own pocket. However, all interests are best served if you remember to approach the seller as a person, rather than a means to an end. Cultivate a genuine interest in the people you contact: they are, after all, fascinating to interact with. Each seller has his or her own needs, problems, talents, goals, interests, philosophy of life. Not all will be willing to give the price or terms you need. But in nearly all cases, they can be enjoyable to meet and talk with if approached in a spirit of friendliness and genuine interest. This makes the work rewarding and fun.

2. Play the Role of Problem-Solver

The don't wanter seller always has a problem that can be solved or alleviated through disposing of the property. Problems create willingness on the part of the seller to be flexible in price or terms (or both). In such cases the buyer can enter the scene as a problem-solver. This role is neither self-deception on the buyer's part nor a case of the exploiting wolf appearing in sheep's

clothing. In fact, the buyer does solve a problem for the seller with the result that all parties win.

To look at it in a somewhat humorous light, the buyer is like a physician who "examines" the patient (seller) for tell-tale clues and symptoms of "don't wanter-itis" and then prescribes certain remedies. Naturally, the powers and resources of the physician are not without limits. He might, therefore, take the following approach (to carry the comparison a bit further):

"I see that you have certain challenges and needs that must be satisfied. I can help to the extent of my resources. And I want to help if I can. If it turns out that my resources are not adequate, I sincerely hope things will go better for you soon."

If the seller is not receptive to your "remedies," then you know that he is not a don't wanter. Don't waste your time with him. Keep on looking for someone you can help.

This problem-solving attitude, if genuine and pervasive throughout the interchange, will infuse your interactions with a sense of humanity and higher purpose. Real estate, after all, is not an end in itself but a means of leading to the solution of people problems. Of course, the attitude of problem-solver is largely an inner affair on the part of the buyer and should not manifest itself in any but the most subtle ways. The point is, you are dealing with a particular group of sellers (the don't wanters), and you will find your work more rewarding if you can cultivate a genuine interest in them as people whom you can help while you are helping yourself.

3. Be Penetrating but Polite

In your questioning you must be thorough. However, thoroughness can be accompanied by good taste, politeness, discretion, and sensitivity to the don't wanter's circumstances. The recent widow or divorcee, for example, should be handled differently from an out-of-the-area seller who simply wants to get rid of a property he does not have time to manage.

4. Pace Your Delivery

Generally speaking, you will want to pace your initial interview with the seller so that it is fairly leisurely and low key. This will put the seller more at ease and give you the opportunity to build trust. In fact, act somewhat like a "don't wanter buyer." Toss in a line like: "You really should keep this property." It will surprise you how the seller will open up.

5. Be Persistent

The final element of the buyer's attitude is acceptance of the fact that he will be playing a numbers game. Of 100 sellers you contact perhaps only a few will be the type of don't wanter you will readily want to deal with. However, it takes only two or three good don't wanters a year to enable you to reach financial independence. Stick with it!

6. Summary: The Five P's of Interaction

The major points for setting the stage can be summarized as follows:

1. **P**eople First

   (In all your discussions, you should remember the win/win philosophy.)
2. **P**roblem-Solving
3. **P**enetrating but Polite
4. **P**aced Slowly
5. **P**ersistence

C. WHAT QUESTIONS SHOULD I ASK?

The preceding section outlined the tone and underlying philosophy of how to approach the seller in the initial contact. The following list includes the basic questions that might be asked. You might want to record these questions on three by five cards for quick reference and notetaking during the interview.

A LIST OF QUESTIONS FOR THE SELLER

Actual Question	Hidden Agenda (reason for asking)	Category
1. Why are you selling?	*—Are you a don't wanter? If so, what kind?*	**A. The Sale**
2. How long has the property been up for sale?	*—You might be more flexible if the property has been up for sale for a long while.*	
3. Have you had any offers?	*—How confident are you?*	
—If so, why have you not accepted any?	*—How flexible are you going to be?*	
—If not, do you have a sense why none have been made?	*—What reactions have others had to your property?*	
4. How long have you owned the property?	*—What is your true vested interest here? (Are you a short-timer who is anxious to get out?)*	
5. How did you arrive at the price?	*—Am I going to get a good deal? Did a real estate agent give you a "free" appraisal? How much is his appraisal worth? Is the appraisal an accredited appraisal? (If so, it will be a good conservative indicator of value.) Is the price inflated?*	
—Have you made major improvements?	*—Are other properties in the neighborhood priced lower?*	
6. Do you have definite plans for the proceeds?	*—If you are planning to put the proceeds into the bank, let me show you how you could earn more interest by taking back paper from me.*	B. Plans Following the Sale
	—If you are going to pay off some debts, could I assume some of your obligations as part of the down payment?	
	—If you need some personal property, could I provide it as part of the down payment?	
	—If you want to invest in other property, could I interest you in a trade?	
	—Could you use professional services as part of the down payment?	
7. (For owner-occupants) Where will you be moving to?	*—Perhaps you could stay on as a tenant (or more into one of my other rental properties), and I could use the prepaid rent as part of the down payment.*	

C. The Property Itself	8. Are there major or minor repairs that are needed?	*—What will my expenses be? Will I be a don't wanter for this property, too?* *—If repairs are needed, the price will have to drop or the property brought up to snuff.*
	9. What are the best (worst) features of the property?	*—How does your view compare with mine? The real estate agent's? The tenants' and neighbors' with whom I have already spoken?* *—If there are problems, the price will need adjusting or the terms relaxed.*
	10. Are you satisfied with the management?	*—If not, I might be able to improve the management and raise the rents.*
	11. Has the quality and rate of occupancy been good?	*—Am I going to be buying an alligator?* *—With upgrading, can the cash flow be improved?*
	12. What rents and deposits does the property have?	*—Can I close on the day rents are due and use the rents and deposits as part of the down payment?*
	13. Do you have any other properties for sale?	*—I might be able to pick up a lead for another purchase or a package purchase.*
D. Current Financing	14. What mortgages are outstanding against the property?	*—If you equity is high, perhaps you would be amenable to a second mortgage crank.*
	15. Who holds the underlying mortgages or notes?	*—If private parties, perhaps the holders of these mortgages or notes will be amenable to a creative financing arrangement (discounting their interest for cash, moving their mortgages, etc.)*
	16. When are the notes due?	*—Perhaps the holders of these notes would be willing to convert the balloons to amortizing notes.* *—Perhaps they would be willing to take a small amount now and postpone the payments for a while.*
E. Future Financing	17. If you must be out soon, you might be more flexible.	*—If you must be out soon, you might be more flexible.* *—If you are in no hurry, you may not be my kind of don't wanter, or you might be willing to give an option.*
	18. Do you need all cash or would you consider monthly payments for part of your equity?	*—Perhaps I can persuade you to take back paper for part of your down payment.*
	19. Would you be willing to secure the loan against another property (rather than the purchased property)?	*—Perhaps I could secure the notes for your equity against another property (or properties) in my portfolio, hence be in a better position to trade, refinance, or sell the property.*

20. Would you reduce the down payment if I gave you a higher price?	*—Which is more important to you: cash or profit? If you are interested in profits, perhaps I can get in for nothing down.*
21. If I gave you all cash and full price, would you close in six months?	*—The property is priced way under the market; perhaps I could set up an earnest-money option and sell my interest for a profit.*
22. What is the lowest price you would accept? — all cash in thirty days?	*What is really your bottom-line price?*

(You can think of many other variations on these questions to suit the particular circumstnaces of the seller analaysis.)

D. WHAT TO DO IF THE SELLER BALKS

1. Assure him of your serious intent and remind him that any buyer who is about to invest such a large sum of money really needs to know as much about the property as possible.

2. If he is a don't wanter, carefully interpret his fears and try to relieve them. Remember your role as a problem-solver and show genuine interest in being of help within the limits of your own resources and powers. Everyone can benefit.

3. If the seller still seems hesitant, ask him politely if the answers to the questions might dissuade you from being interested in buying his property.

E. A FINAL WORD ABOUT SELLER ANALYSIS

This is an important step of the purchase but should not be confused with negotiations. Although the seller may begin to mention numbers here, you should not make any commitments or indicate your willingness to buy or reveal any part of your forthcoming offer.

Of course, the better part of genius is common sense. If things suddenly fall in place to your liking, go ahead and make an offer on the spot. You don't succeed in slow motion.

And here is a concluding point: Not only am I as a buyer analyzing the seller at this stage, but he is analyzing me. Oftentimes the seller becomes more and more flexible as he sees he can trust me. The only way the seller will consider the kinds of creative financing techniques we offer him is if he trusts us. Throughout the entire purchasing process you should strive to build trust with the seller.

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SECTION G

Location Analysis

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Location Analysis



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G

Location Analysis

Location analysis is one of the most important aspects of an investor's decision to buy real estate. It has been said that the three most important rules for buying an investment property in real estate are:

(1) Location!
(2) Location!
(3) Location!

I have read recently in several books that the authors feel that location is not as important as terms. I want to hereby heartily disagree. Location is one of the most important things that you need to examine, because if you don't, you may find yourself in the situation where you become a don't wanter for a piece of property because you are attracting the wrong kinds of tenants.

1. We need to find properties that are going to consistently increase in value. This can only be done if you buy property in the right kinds of locations.

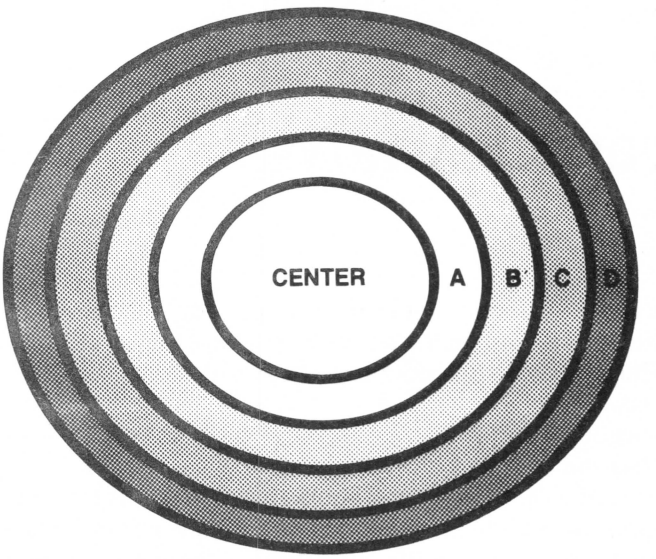
2. Since ours is a long-term goal, we must find properties that cause us the least management hassle. Poorly-located properties cause don't wanter-itis. Life is short enough as it is; don't make it miserably short.

A. THE CONCENTRIC CIRCLE THEORY

As I analyze locations, I do it by referring to a concentric circle theory (see the illustration). I try to analyze in my mind why the tenants of this particular property live here. Is it because it is close to their place of employment? Is it because it is located close to mountains, streams, or parks? Why do my tenants live in this particular property? The factor which makes my tenants want to rent the property is at the center of my concentric circle. Those properties that are located closest to that center of the concentric circle I call my "A" properties. The properties that are located in "A" areas will have higher rents, will have higher appreciation rates, will have lower vacancy rates, will have more desirable tenants. The properties that are located in area "D" will have lower occupancy rates, higher expenses, lower class tenants, will have lower prices of course, because they will be low in demand, and they will also be appreciating much less. Obviously, it will be difficult for me to find a don't wanter in an "A" area. It may take more looking, but if I could find a property in an "A" or "B" area, I will know that that property will have the best chance for the long-term kind of growth that I am going to need for my investment program.

1. Long-term Versus Short-term Investments

Now with respect to this analysis, it is important to understand that I am not suggesting that you do not buy property that is in poor locations. I am suggesting that you do not buy those kinds of property for long-term growth. And if you are going to buy a property in a "D" location because you have located a price and terms that are so good you can't pass it up, then you



CONCENTRIC CIRCLE THEORY

should purchase it with the object in mind that you should turn it over quickly for a quick profit or sell it with no down payment and carry a profit in paper in order to generate a monthly cash flow. Invest very little money in "D" location properties and insist that your money be turned over quickly so that it can be reinvested into "A" and "B" type properties.

What kinds of things can be the center of the concentric circles that I am talking about? Shopping centers in downtown areas, universities, and factories and places of large employment. I am just asking you to analyze properly all the factors that go into a tenant's decision to rent your particular property and determine whether or not it is in a good location.

2. Stability: The Most Important Factor

The most important factor you should try to determine as you buy a property is whether the neighborhood is a stable and growing neighborhood or a declining and a deteriorating neighborhood. Ask yourself, "Will I be able to hold this property for five years without worry or fear that the neighborhood will decline in value?"

3. "The Worst Acceptable Property in the Best Acceptable Neighborhood"

I try to buy the worst acceptable property in the best acceptable neighborhood. In other words, I am trying to find a property that is less fancy or smaller or not quite as nice as the properties next to it. If I can find that type of property, say a three-bedroom home in a four-bedroom home neighborhood or a 1200-square-foot house in a neighborhood of homes that are 1600 square feet, I will find that the prices of the larger homes around me will tend to draw the price of my property up. If, on the other hand, I purchased a property in a poor neighborhood and I buy the best property in a poor neighborhood, I will find that the properties around me will tend to pull my price down.

4. What to Look For

What kind of things do I look for as I am driving through the neighborhood? I'm looking for the touches that show pride of ownership. The way people take care of their lawns and shrubs, the neatness of the yard, etc. I look to see what kind of people are walking the street and so on.

B. GETTING PROFESSIONAL OPINIONS ABOUT THE NEIGHBORHOOD

Now whom can you call to answer your questions about the neighborhood?

1. Real Estate Agents

The real estate agents are probably the best and cheapest source of information. They can tell you where to go, which neighborhood to concentrate in, where the concentration of don't wanters is.

2. Professional Property Management Companies

Professional property management companies can be notified, especially if you are looking at an apartment building. They will tell you what their experience has been in renting apartment buildings in that particular area of town. They can tell you what vacancy rates they have experienced. And they usually are willing to share this information with you, because it is their job to locate new clients all the time for their apartment management. And if they seem to give you a favorable answer, perhaps you might come to them for some of your property management in the future.

3. Managers of Adjacent Properties

You can talk to managers of adjacent properties and ask them what the problems have been, ask them what their vacancy rates have been, ask them what their opinion is of the neighborhood and of the particular location.

4. Police Department

You can call the police department. You will find that most all modern police departments have a listing of all areas and all quadrants of their city. They know where the most complaints and the most robberies occur, and they can steer and guide you into the neighborhoods where there is less crime.

5. Local Planning and Zoning Officials

I also find it is an excellent idea to visit with the local planning and zoning officials. They are public appointed officials and in most instances are most happy to divulge information to you about your particular city. They can tell you which areas of the city have need of careful attention. And I also find that if I can get to know the members of the planning and zoning commission, they are knowledgeable about areas of the city that will be developed in the future. And they can tell you the information about which areas of town will be more valuable in the future, which corner, which area will be commercially zoned. Most of this information is a matter of public record, and they are more than happy to share it with you. But very, very few people, just a small percentage, really know what's going to happen. Most cities have five- and 10-year plans, and sometimes in large cities it is known up to the year 2000 what they are going to do in several areas of the city. This is important information; it's profit-making information, and you should avail yourself of it.

C. KEY WORD FOR TESTING LOCATION: POWER

There is a key word for testing location, and that is "P-O-W-E-R."

Careful attention to the following factors will put power into your decisions:

P Proximity to amenities, shopping centers
O Opportunity to raise rents (competition density not too high)
W Worst property in best neighborhood, not best in worst
E Employment configuration of area adequate to supply tenants
R Rent level of area in keeping with mortgage arrangement (rents sufficient to cover the mortgage payments)

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SECTION H

Financial Analysis

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Financial Analysis

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Financial Analysis

H

A. WHY REAL ESTATE IS THE IDEAL INVESTMENT

Real estate is the ideal investment. It offers attractive opportunities no matter what the economic climate is. It provides the satisfaction of property ownership. Since land is at a premium, real estate is a high demand item. Furthermore, if it is carefully selected, it will generate income for you. It offers tax shelter. As you make your payments, you get equity build-up. It also appreciates in value and its greatest benefit: it can be purchased with little or no down payment. That is leverage.

Real Estate Motto:
"IT'S IDEAL"

Advantages of Real Estate as an Investment

I Independent of Economic Conditions (always good opportunities)
T True Satisfaction of Property Ownership
S Supply/Demand Relationship is Optimal ("They ain't makin' any more land.")

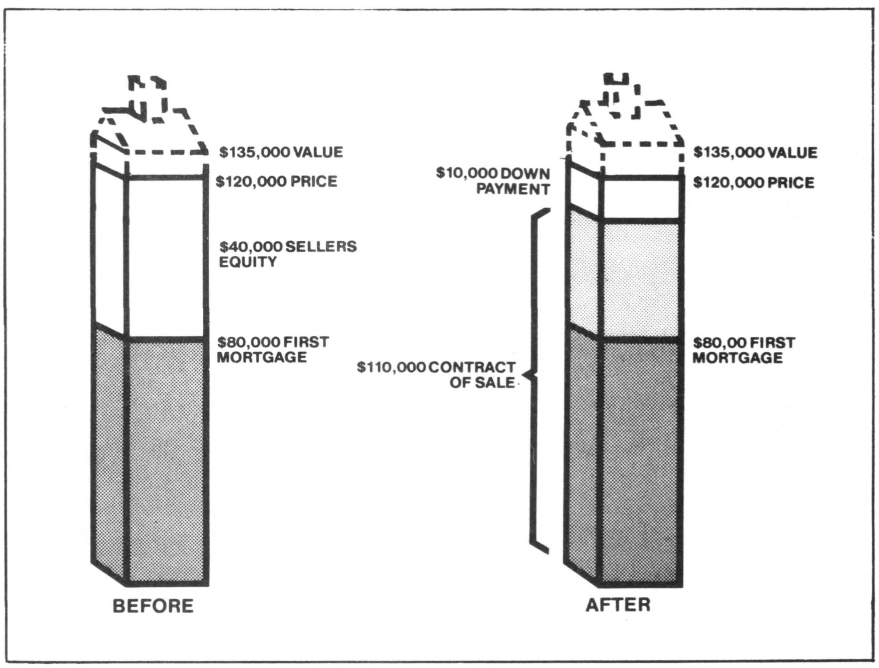
I Income Producing
D Depreciation and Interest Tax Advantage
E Equity Build-up
A Appreciation
L Leverage (using other people's money)

B. A CASE HISTORY: WOULD YOU BUY THIS PROPERTY?

Let's analyze an apartment building to see whether or not we might be interested in purchasing it. Take for example the building depicted in the box on the next page. It's a five-unit apartment building, rents for $400 a month, expenses are 35 percent of gross income, there is a 4 percent vacancy rate, mortgage payments are $826 a month with 11 percent interest, and there is $30 a month extra income from vending machines. As you look at this piece of property, you can see that the seller is willing to sell it for a $10,000 down payment. And he's willing to carry a contract of sale, or he's willing to carry the financing. Sometimes this is also called a wrap around mortgage. And he will leave his $40,000 equity in the property and receive monthly payments on it for the next 25 years. The question I'd like to ask you is, "Does this property have a positive or negative cash flow on a monthly basis; and if you had $10,000, would you or would you not buy this piece of property?"

1. The Annual Property Operating Data Form

How many of you would buy this property, and how many of you would not? To help you, I have included an analysis form that anyone can use. It is simple and easy to understand, and it has blanks for every important piece of financial information that is needed. Be conservative! This form helps you become conservative by reminding you of things that you should not forget to examine.



5–UNIT APARTMENT BUILDING

Facts:

- 5-unit apartment building
- rents are $400 per month
- expenses are 35% of gross income in this example (current average is closer to 40%).
- 4% vacancy rate
- mortgage payment is $826 per month with 11% interest
- $30/month extra income from vending machines

2. Detailed Analysis of the Case History

This form may be available through the local Real Estate Board. Note the major items in the data form.

Financing: Information about the existing and potential financing are recorded in the upper right hand corner. In this instance, there is a spread of one-quarter percent in the interest (from 11 to 11.25 percent) and an "overhang" of five years on the period of repayment.

Gross Income: (Items 1 through 5): In this case, the gross scheduled rental income ($24,000) is augmented by $360 ($30 per month from vending machines) but decreased by $1,200 (vacancy and credit losses). Check with a real estate agent on the vacancy rate for the area. Speak with tenants concerning the rent situation. The gross operating income is $23,160.

Operating Expenses: (items 6 through 31): Watch especially the following:

- Item 7, accounting and legal fees are needed to figure taxes, assure the correctness of the operation, etc.
- Item 9, Property Insurance—send over your own insurance man and make sure you are properly covered. Get bids for the best rate!
- Item 10, Property Management—figure on about 7 percent of the gross rental income (higher in some areas; up to 10 percent).
- Item 15, Real Estate Taxes—be sure to figure on the basis of next year's assessment.
- Item 16, Repairs and Maintenance—figure on 4 to 10 percent of the price. Ask to see the latest income tax return (where the expenses are no doubt reflected at the highest rate).
- Item 23, Supplies—minor items, perhaps up to 1 percent of gross operating

income.

- Item 24, Utilities—arrange with the seller to have access to utility bills for the past 18 months. It would be preferable if the building were set with separate meters so that the tenants could pay their own utilities. In our example, the tenants pay their own gas and electricity, but the landlord pays for sewer and water.
- Item 31, Total Operating Expenses—a critical figure. Will probably be around 40 to 50 percent of the gross operating income, probably around 40 percent. If the seller tells you it's below 30 percent, be highly suspicious (unless the building is new, and your analysis shows low taxes and tenants paying all utilities). Take care that the "bargain" property does not turn out to be a haven of "deferred maintenance."
- Item 32, Net Operating Income (item 5 less item 31)—a critical figure needed to calculate the capitalization rate for buildings of five or more units.
- Item 33, Total Annual Debt Service—in this case $1,098 per month for 12 months.
- Item 34, Cash Flow Before Taxes—the bottom line. In this case the cash flow return on your $10,000 down payment is 7.2 percent. If the cash flow is negative, watch out! You may have an alligator unless you can improve the flow soon (raise the rent for example).

C. CALCULATING THE RATES OF RETURN FROM AN INCOME PROPERTY

(Refer to summary sheet on page H-8.)

1. Income (Cash Flow)

In this case the cash flow return is 7.2 percent. (A more realistic figure in today's market would probably be 2 to 3 percent.)

2. Depreciation (Tax Savings)

Real estate investment provides one of the few remaining tax shelters. In our example, the value of the property is $80,000 (excluding the land). If it is depreciated over 15 years using the Accelerated Cost Recovery System introduced under the Economic Recovery Tax Act of 1981, the first year's recovery (depreciation) is $9,600 (assuming the property was purchased in the first month of the year). To figure the tax advantage, reduce this amount by the cash flow and the loan reduction, and the resulting tax loss can be written off against your other income. If you were in the 30-percent bracket, the savings would be $2,372 in our example. This is a rate of return of 23.72 percent on your investment (down payment).

It is critical to consult a competent tax accountant in figuring the depreciation (cost recovery) and tax loss, because the tax laws are changed from time to time at the Federal level.

3. Equity Build-up

This is the principal paid on the loan during the course of the year. The principal will, of course, be returned to you as you sell the property. With the $10,000 down payment, the return for this item is 10.04 percent.

4. Appreciation

At 10 percent annually, this would amount to $10,000, and the return on investment could be 100 percent!

In all, the total rate of return for our example would be the total of these four rates (1 + 2 + 3 + 4) or 140.66 percent! If you believe in the parable of the talents, you can feel good about this return on your investment.

SAMPLE

Annual Property Operating Data

Purpose _____ Date _____

Name _____

Location _____ Price $ _____

Type of Property _____ Loans $ _____

Assessed/Appraised Values Equity $ _____

Land	$ _____	%
Improvement	$ _____	%
Personal Property	$ _____	%
Total	$ _____	100 %

Adjusted Basis as of _____ $ _____

FINANCING

	Balance	Payment	Period	Interest	Term
Existing	$			%	
1st	$			%	
2nd	$			%	
3rd	$			%	
Potential					
1st	$			%	
2nd	$			%	

		%	2	3	Comments
1	GROSS SCHEDULED RENTAL INCOME				
2	Plus: Other Income				
3	TOTAL GROSS INCOME				
4	Less: Vacancy and Credit Losses				
5	GROSS OPERATING INCOME				
6	Less: Operating Expenses				
7	Accounting and Legal				
8	Advertising, Licenses and Permits				
9	Property Insurance				
10	Property Management				
11	Payroll - Resident Management				
12	Other				
13	Taxes-Workmen's Compensation				
14	Personal Property Taxes				
15	Real Estate Taxes				
16	Repairs and Maintenance				
17	Services - Elevator				
18	Janitorial				
19	Lawn				
20	Pool				
21	Rubbish				
22	Other				
23	Supplies				
24	Utilities - Electricity				
25	Gas and Oil				
26	Sewer and Water				
27	Telephone				
28	Other				
29	Miscellaneous				
30					
31	TOTAL OPERATING EXPENSES				
32	NET OPERATING INCOME				
33	Less: Total Annual Debt Service				
34	CASH FLOW BEFORE TAXES				

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Prepared by _____

SAMPLE

Annual Property Operating Data

Purpose _____
Name Ridgeview Apartments
Location 1005 Apartment Row
Type of Property 5 units
Assessed/Appraised Values

Land	$ 4,800	20 %
Improvement	$ 19,200	80 %
Personal Property	$	%
Total	$ 24,000	100 %

Adjusted Basis as of _____ $_____

Date August 18

Price $ 120,000
Loans $ 80,000
Equity $ 40,000

FINANCING

	Balance	Payment	Period	Interest	Term
Existing	$ 80,000	826	mo.	11 %	20 yrs
1st	$			%	
2nd	$			%	
3rd	$			%	
Potential 1st	$ 110,000	1098	mo.	11.25%	25 yrs
2nd	$			%	

		%	2	3	Comments
1	GROSS SCHEDULED RENTAL INCOME			24 000	5 x 400 x 12
2	Plus: Other Income			360	
3	TOTAL GROSS INCOME			24 360	
4	Less: Vacancy and Credit Losses	5%		1 200	
5	GROSS OPERATING INCOME			23 160	
6	Less: Operating Expenses				
7	Accounting and Legal		300		
8	Advertising, Licenses and Permits		500		
9	Property Insurance		600		
10	Property Management	7%	2 316		
11	Payroll - Resident Management		600		
12	Other				
13	Taxes-Workmen's Compensation				
14	Personal Property Taxes				
15	Real Estate Taxes		1 500		
16	Repairs and Maintenance	5%	1 158		
17	Services - Elevator				
18	Janitorial				
19	Lawn -mgt. firm				
20	Pool and resident mgr. do this				
21	Rubbish -tenant pays				
22	Other				
23	Supplies	1%	240		
24	Utilities - Electricity				
25	Gas and Oil				
26	Sewer and Water		1 800		
27	Telephone				
28	Other				
29	Miscellaneous		250		
30					
31	TOTAL OPERATING EXPENSES	40		9 264	
32	NET OPERATING INCOME			13 896	
33	Less: Total Annual Debt Service	✓		13 176	1098 x 12
34	CASH FLOW BEFORE TAXES			720	

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CALCULATING THE RATES OF RETURN FROM AN INCOME PROPERTY IN THE U.S.:

A. **Income** (cash flow):

$$\frac{\text{Cash flow}}{\text{Down payment}} = \frac{720}{10{,}000} = 7.2\%$$

B. **Depreciation** (tax savings):

Under the Tax Reform Act of 1984, 18-year accelerated cost recovery is allowed for properties placed in service beginning March 15, 1984. (One also has the option of using 18, 35, or 45 year straight-line depreciation.) The example below shows how the "Accelerated Cost Recovery System" works for the first year of ownership, assuming a full-year's recovery. (The accelerated method is calculated using 175% of the straight-line declining balance method. Consult a competent tax expert for details and guidance, since the government is constantly changing the guidelines.)

In our example:

Cost recovery = value of building without land ÷ 18 × 175%
= 96,000 ÷ 18 × 175% = $9,333

Tax loss = cost recovery minus cash flow and loan reduction (see item C)
= $9,333 − 720 − 844 = $7,769 (first year)

$$\text{Tax savings} = \frac{\text{tax loss} \times \text{tax rate}}{\text{down payment}} = \frac{6{,}084 \times .30}{10{,}000} = 23.31\%$$

C. **Equity buildup:**

$$\frac{\text{*Loan reduction}}{\text{Down payment}} = \frac{844}{10{,}000} = 8.4\%$$

*This is calculated using a Hewlett-Packard 12C calculator or other similar product. You may need special help with this.

D. **Appreciation:**

$$\frac{\text{Building cost} \times \text{appreciation rate}}{\text{Down payment}} = \frac{135{,}000}{10{,}000} \times 5\% = 67.5\% \text{ (using a conservative 5\%)}$$

TOTAL RATE OF RETURN FROM INVESTMENT IN FIRST YEAR:

		With Leverage ($10,000 down)	**Without Leverage** ($120,000 down)	
I —	Income (cash flow)	7.2%	11.6%	(NOI = cash flow!)
D —	Depreciation (tax savings)	23.31%	−1.14%	$\frac{(9{,}333 - 13{,}896 \times .30 \times 100)}{120{,}000}$
E —	Equity buildup	8.4%	0	
A —	Appreciation	67.5%	5.00%	
TOTAL RETURN		106.41%	17.76%	

Note: To calculate the rate of return for a Canadian property, the major adjustment comes in Item B, "Depreciation."

D. DETERMINING THE VALUE OF THE PROPERTY

Determining value from financial information.

1. The Gross Rent Multiplier

Different areas have different rules of thumb for determining property values. California, for example, uses the gross rent multiplier formula. Let's say you notice in the newspaper an eight-unit apartment building advertised at "8 ×" or eight times gross. This means that the value of the property is eight times its gross scheduled income. If the rent is $200 per unit, the gross scheduled income would be eight units times $200 per month times 12 months or $19,200. The value of the property would be 8 × $19,200 or $153,600. If it has a high gross rent multiplier, then its price is high. (In other words, if the gross rent multiplier is 10 or more.) If it has a low gross rent multiplier, then the price is low. If its gross rent multiplier is seven or less, then it's probably a very good price.

a. Disadvantage of This Approach. It is not wise to analyze the value of a property by using a gross rent multiplier because the gross rent multiplier does not take into account expenses, and expenses can be a major portion of the investment. Therefore, if an agent is determined to give you the gross rent multiplier of the property, you can understand what they mean, but you must be very wary of accepting gross rent multipliers as being the true value of the property.

2. Capitalization Rate: The Only True Way of Calculating Value

The capitalization rate is the only true way of calculating value. All serious professional investors use capitalization rates. The capitalization rate is a way of determining return on investments. I have a $100,000 building which I want to buy, and it has an income after expenses of $8,000 a year. And if I had purchased this property of $100,000 in cash, then this property would generate for me $8,000 worth of before-tax income or 8 percent return on my investment.

a. Applying the Formula to Our Initial Example (5-unit building)

$$V = \frac{I \text{ (net operating income)}}{R \text{ (capitalization rate)}}$$

—or—

$$R = \frac{I \text{ (n.o.i.)}}{\text{Value (price)}}$$

$$R = \frac{13{,}856}{135{,}000} = 10.3$$

Range of value in capitalization rates

0 . . . . . 5 . . . . . 10+

low end high end

Thus, we would be extremely interested in this property.

b. The Range of Cap Rates. It used to be in the past that an investor would not invest his money into an apartment building unless he could make at least a 10 percent return on his investment. In other words, the net operating income, or line 32 of our previous form, is divided by the value of the property, which is $135,000. If that did not equal the 10 percent (in this case $13,896 divided by $135,000 equals 10.3 percent), then he would not buy the property. However, in recent years the values of properties have been increasing due to demand and inflation faster than the rate of operating income has been increasing. This has caused the capitalization rates to decline. In other words people are willing to buy a property that has an 8 percent capitalization rate or a 7 percent capitalization rate. In some areas of the United States, especially California and Washington, D.C., also in the Canadian province of Alberta, some investors are even willing to purchase apartment buildings that have a 5 and 4 percent capitalization rate. What this means is that people are looking more to an increasing value of property than they are looking towards income. Obviously, this trend has caused real estate prices to jump drastically. As people have expected prices automatically to increase, they have sacrificed cash-flow return in anticipation of high appreciation profits. Since rents haven't kept pace with property values, cash flows from real estate are low, and can even be negative, depending on financing.

What you must remember is not to get caught up in the feverish purchase of highly overpriced properties just for the sake of investing. Each property must be carefully analyzed on its financial merits before an offer is presented or accepted.

c. A Warning About "Speculating." You must understand that to be an investor in real estate, you must completely eliminate speculation from your mind. To speculate on a piece of property is to bet on its value increasing without consideration of the price that you purchased it at. I like to say that when I invest my money in a piece of property, I have to know that that property is purchased at least at market price and hopefully below. If I invest more than 10 percent of my cash or anyone else's, I need to know that that property is below the market price. If I don't, then I am speculating; if I do, then I am investing.

d. An Acceptable Cap Rate. One way to invest in income property is to determine what its capitalization rate is. Be very careful what you buy. The capitalization rate is going to vary from city to city, from location to location in your city, and from area to area. But as a general rule, you'll find that if ever you divide the net operating income of a piece of property by its value and you come out with a figure less than 7 percent, you're going to have to be very careful that you're not paying too much for that piece of property. The only way that you can feel comfortable that the price is right is if the rent is out of line. Maybe the rents are too low. Maybe they can be raised to make this property value seem more in line with this capitalization rate. If you find a capitalization rate that is above seven, then you are going to know that the value of that property is more in line with its market price. You will also find that if you ever find a property that has a capitalization rate that is less than seven, you are going to have great probability for negative cash flows. A property with a capitalization rate above seven will have greater probability for positive cash flows.

3. The Phone Interview: A Quick Way to Test the Cap Rate. There is a certain process that you go through on the telephone for finding out this kind of information. Let's walk through that together. "Hello, Mr. Seller, I under-

stand you are selling a nice five-unit apartment building, and the five units are rented out at $250 a month. Is that correct?" "Yes, it is." "What is your vacancy rate?" "I don't have any vacancy." Automatically you know that that is not correct because there is always a vacancy rate. There is a vacancy whether it be in lost income or loss of time rented when one tenant moves in and the other moves out. There is always going to be some sort of vacancy, and if there is not a vacancy rate, then he's wrong. Now, if he says that he made any extra income from his rental such as the rental of pet fees or furniture or parking spaces or whatever else, then we include that also. "What were your expenses last year?" And he tells us that his expenses were $3,000. Well, we can do our own little spot checking to see if he was right. Three thousand dollars divided by an income of $15,000 gives us a figure of 20 percent. "Do you mean to tell me that 20 percent of your income was spent on expenses? Are you sure about this, Mr. Seller?" Either he's right, or he's wrong; but in our operation of the property, we're going to have to assume at least 40 percent expenses, so we'll figure 40 percent expenses, and we'll subtract $6,000 from our gross operating income of $15,000, and we come up with a net operating income of $9,000. "Now what did you say the price of your property was again, Mr. Seller—$100,000?" Nine thousand net operating income divided by $100,000 equals 9.0.

a. Reactions to a Favorable Cap Rate. Am I going to be interested in this property? Yes, I am, extremely. The property is already sold by now because that capitalization rate is so good it shows that the price is right and the income is right and shouldn't last very long because there are a lot of investors looking for that kind of opportunity. The only thing I need to take into account is whether the property itself is in good condition, whether the location is right, and whether the seller is a flexible seller.

b. Reactions to an Unfavorable Cap Rate. Now what happens if I do my capitalization rate analysis and I get a net operating income of $4,950 divided by $100,000 price? Then I have a capitalization rate of somewhere in the neighborhood of five. Is that going to be very thrilling to me? Well, I'm going to know that that is going to give me a higher probability for negative cash flows, and I may have to check around the neighborhood to see if that's what the properties are selling for. I might not be too thrilled about buying property that has such a low capitalization rate. The property itself may be an excellent property; the rents are just too low. So I have to make sure that the rents are in the market before I pass this one up. In most cases the rents are pretty close to market, and I can know by my capitalization rate analysis whether it's an interesting investment or not.

4. Where Won't the Cap Rate Work?

Incidentally, the capitalization rate analysis does not work very well with properties that are duplexes and four-plexes and other small units of four or five units because the demands for such units have increased the prices so drastically that the capitalization rate formulas are very low. People have been speculating on the prices of these properties because they are down in the area where there is the greatest demand. So the only way that you can tell whether you are making money on a four-plex or a duplex is to compare its price with the prices of other properties that are comparable to it which have sold recently in the same area. But for units that are larger than five or six units you can use the capitalization rate formula, and you can be fairly accurate with the information that I have given you.

If you are a beginner and don't quite understand the valuation process, hire a professional appraiser, or use a real estate agent who knows his investment market well. The best real estate agent to deal with will have a

CCIM designation (Certified Commercial Investment Member). This is a strenuous program of certification which is granted by the Realtors' National Market Institute. For a listing of all CCIM real estate agents in your area, write RNMI, 430 North Michigan Avenue, Chicago, IL 60611, or call (312) 440-8000. Through practice your confidence will grow, and you will be able to make accurate market-value estimates yourself.

E. HOW TO RAISE THE VALUE OF THE PROPERTY

Now, how do you raise the value of the property?

1. Raising Rents

When you raise the rent on a property, you automatically raise your net operating income if you can keep your vacancy rates constant and if you can keep your expenses constant. If you raise your net operating income, you will automatically raise the value of the property. If properties are selling for a capitalization rate of 7 percent, then you can raise the value of your property by anywhere from $10 to $15 for every dollar of increase in the net operating income. A dollar increase in the amount of rent you get increases the value of your property by $10 to $15. If I can increase my rent by $10 a month over a ten-unit building, which is as much as $1,200 a year, I have increased the value of my property by as much as $12,000 and maybe even more, depending on my market area. You've raised the value of your property by raising the rents. And you can raise the rents in your property by increasing the attractiveness of your apartment building. If you fix up a property and thereby attract tenants who are willing to pay higher rents, you have automatically increased the property value. (Note: in some areas, legislation regarding rent controls may affect your ability to raise rents.)

2. Lowering Expenses

In addition to raising rents, you can also increase your net operating income by lowering expenses, for example, having your tenants pay utilities instead of you paying utilities. Therefore, when you are buying an apartment building, make sure that its capitalization rate is seven or higher. If it is less than seven, check your marketplace. Are people really paying less than seven for a piece of investment property? If they are, you may be justified in paying a higher price for a piece of property, but you must realize that you will start to have negative cash flows.

3. Increasing the Effectiveness of Property Management

Effective property management is the key to long-term ownership of real estate. You should follow the "Ten Commandments" of property management:

a. The Ten Commandments of Management.

1. Choose the right tenant!
- Credit checks are important. Your apartment owner's association can help you in this respect.
- Insist upon references from previous managers. One call can save you a lot of grief.
- Check their present living quarters (if possible) or have a look inside their car. Will they take care of your property the way they take care of their present apartment?
- Does your prospective tenant have an adequate job? Verify.
- Does he have credit cards?
- Can he fix major or minor repairs? Offer lower rent.
- Can you feel right about renting to this family?

There are two kinds of vacancies: One where the property is vacant. One where the property is occupied by a deadbeat. Which would you rather have?

2. Always a deposit!
- Up to one month's rent in advance.
- Not to be counted by the tenant as rent at any time in the future. It is a security deposit.
- Not returned until 15 days after the property is vacated to insure against late utility bills and unnoticed damage. (Review local laws on this subject.)

3. Rent is due on time!
- Late fee to be deducted from security deposit if five days past due. Better still, use a discount system—a fixed amount is deducted from the rent for prompt payment.
- Rent is a top priority item. Then comes food. Then comes clothing. Don't let the tenant feel as if you will be lenient with the payment of rent; otherwise he will change the priorities, and the motorcycle will get paid first, leaving you out in the cold until next paycheck. Establish with him at the very beginning that you have a mortgage payment to make, and you can't wait—because your bank doesn't wait for you!

4. Minor repairs are yours—I'm busy!
- You don't have time to fix every leaking faucet. Delegate this to the tenant at the outset and sleep in peace.
- Try to set tenants up on a "self-management" program. They take care of all maintenance under $200 in exchange for special benefits (a discount on the rent, an option to purchase, first right of refusal, etc.). Discounts come in various forms, e.g., a percentage (such as 8 percent per month), a fixed amount (such as $50 per month), or twelfth month free each year.

5. Inspection regularly—at least once a month!

6. Get a lease or rental agreement with teeth!
- Obtain copies of good local leases from a good property management company or the Apartment Owners' Association (in Canada, the Landlords' Association).

7. Cut turnover!
- Thirty-day notices before leaving.
- Long-term relationships with present tenants.
- Proper advertising.
- You may even consider giving a small percentage of the eventual profit to a good long-term tenant. This cuts turnover, gives you responsible management for out-of-state owners, and can even cut negative cash flows.

8. Always inspect property with prospective renter and prepare an inventory of any existing damage.

9. Tenants pay all utilities if possible to cut escalating fuel costs; also, mows the lawn.

10. Once you reach your breaking point (with one or 100 units), get professional management. They know what they are doing. (Obtain copies of the excellent management books by Leigh Robinson and Al Lowry listed in the bibliography. Learn how the experts do it.)

Creating Wealth

WITH LITTLE OR NOTHING DOWN

Manual

The Nothing Down System of Creative Financing in Real Estate Investments

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SECTION I

Market Analysis

Robert G. Allen

M.B.A.

IN COOPERATION WITH

Richard J. Allen

Ph.D

I

Market Analysis

There are two types of market analysis. The first type of market analysis is that which has to do with the building itself, the property. The second type of market analysis is that which has to do with the current money market picture.

A. ANALYSIS OF THE MONEY MARKET

Let's talk about the money market first.

1. The Important Questions: Shopping for the Best Deal

If you are buying in the United States, it's important to do some checking at savings and loans, at commercial banks and other lending institutions, to find out what the money market situation is really like. At savings and loans we can borrow money on conventionally-financed properties, but it's very difficult to find this kind of money in periods of tight financing. Even in tight money markets, however, there is always money available for F.H.A., Fannie Mae, and V.A. government-sponsored loans. We need to know where these loans can be obtained, which banks are giving them, what the ratios and interest rates are, what points are being charged, etc. I need to know where I can obtain non-owner occupied loans. What ratios of value to loan can I obtain? Can I qualify for a loan like that? I need to know that kind of information really before I start looking for my investment so that I can be prepared when I talk to the seller about the kinds of financing I can obtain if I need financing at all.

In Canada, test the money market situation by checking with credit unions, trust companies, commercial banks, and other lending institutions. When the money situation is tight, one can usually still find money available through the Central Mortgage and Housing Corporation (C.M.H.C.) or through the provincial government sponsored loans.

2. Sources of Information

a. Title Companies (U.S.) or Land Titles Offices (Canada). In my area of the United States where title companies do a major amount of business, there is a lot of competition between title companies, and several of them prepare a money market sheet that shows how current banks are lending and what the interest rates are. Therefore, on a very short examination you can determine which are the best banks and which are offering the best rates and points.

In Canada the various provincial governments operate Land Titles Offices with responsibility for certain areas. This information can be expanded by data available from municipal assessors' offices. There are certain legal controls as to the extent of information that may be provided. Still, it pays to become informed to the extent possible.

b. Collecting the Data Yourself. If your area does not have a title company that can do this type of service for you, do that kind of work yourself by calling up 15 or 20 different lending institutions in your area and asking them the pertinent questions. It is a good exercise; it helps you get prepared for the marketplace, and it eliminates a lot of the fear that has stopped many people from buying real estate.

B. THE PRICE OF THE PROPERTY: HOW DOES IT COMPARE?

The second type of market analysis is whether or not the property that you are buying is competitively priced compared to other properties in the marketplace.

1. Learning to Compare Unit Prices

If we're talking about houses, we need to know what the square footage is; we need to know how many bedrooms there are; we need to know how many properties there are in the immediate vicinity that are selling for prices comparable to the price of the property that we are looking at.

2. Eliminating Risk by Comparative Analysis

If I am looking for apartment buildings, I need to know what people are paying per unit. Are they paying $25,000 a unit; are they paying $50,000 a unit for a standard two-bedroom size apartment unit? The more you know your marketplace the more money you are going to make. It's as simple as that.

We need to know if the seller has looked at the marketplace. It's a good idea to go into your marketplace and to choose 10 or 15 different properties before you buy and analyze them compared to the property that you are buying to see whether or not you are paying too much for it. This is one of the most important things I can recommend to you. Money is made in real estate investments when the real estate investor learns how to understand the marketplace, learns when and when not to buy, and learns when he is making money and when he is paying too much. That is one of the most important exercises you can learn. And all it takes is some time and exposure in the marketplace. When you locate a property that is $10,000 below the marketplace and you can determine that it is below the market, you can act quickly. If you don't act quickly, someone else is going to get it. But if you don't know if it's underpriced, you won't act quickly, and you are going to lose that profit.

C. SOURCES OF INFORMATION

There are several sources of information.

1. Real Estate Agents and MLS Sold Books

Real estate agents are probably the best. They know the marketplace better than anyone else because they are in it at all times. They also have information that is compiled in multiple listing sold books, which is a listing of all the previous three months' sales, including location and sales price. That is an excellent way of determining quickly what properties have been selling for in the past three months.

2. Asking Owners

I can also stop at "for sale by owner" signs and ask these people how they determined the price of their property. Did they determine it by picking a figure out of the air that they would like to get? Did they figure it by going into their own neighborhood and comparing their property with other properties? By driving through a neighborhood and asking resident owners, I can usually determine within a very short period of time and within a few thousand dollars whether or not my property is priced too high or too low.

3. Appraisers

If I feel uncomfortable about the analysis that I have done on my piece of property, I can hire an appraiser. They can charge me anywhere from $50 to several hundred dollars to do the same kind of analysis, but it gives me a more professional yardstick on the market price. In some instances if I really am conservative, I can make my offer to the sellers subject to an appraisal by a conservative appraiser so that I know that I'm not going to pay more than what that appraisal price is.

D. USING THE COMPARATIVE MARKET ANALYSIS FORM

To help you with your analysis of the marketplace, we have provided a form below called the Comparative Market Analysis Form which gives you an area to mark in your comparably priced properties. Those that are on the market now, those that have sold the past twelve months, and in some instances those that have expired in the past twelve months. The best source to obtain this information quickly and cheaply is from a local real estate agent.

COMPARATIVE MARKET ANALYSIS FORM **NOTHING DOWN SEMINAR MANUAL**

Subject Property Address _____ Date_____

Information on other properties which are located in the same general area and have the same approximate value as the subject property:

FOR SALE NOW	Bed-rooms	Baths	Den	Sq. Ft.	Mtgs.	Price	Days on Mkt.	Terms
SOLD PAST 12 MONTHS								
EXPIRED PAST 12 MONTHS								

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SECTION J

Property Structure Analysis

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Property Structure Analysis

J

A. AREAS WHERE COSMETIC IMPROVEMENTS MAY ENHANCE THE VALUE OF THE PROPERTY GREATLY WITH ONLY MODEST INVESTMENT ..... J- 3
B. AREA WHERE STRUCTURAL DEFECTS AND MAJOR DEFICIENCIES COULD BE VERY COSTLY. BEWARE! ..... J- 3
C. SOME TIPS ON IMPROVEMENTS ..... J- 4
D. PUTTING THE PROFESSIONALS ON YOUR SIDE ..... J- 4
E. REAL ESTATE AGENTS ..... J- 5
F. THE NOTHING DOWN PROPERTY SELECTION MATRIX ..... J- 6



Property Structure Analysis

The following checklists might be of help to you in analyzing the property you are considering:

A. AREAS WHERE COSMETIC IMPROVEMENTS MAY ENHANCE THE VALUE OF THE PROPERTY GREATLY WITH ONLY MODEST INVESTMENT

	Needs Improvement	
	Yes	No
1. Do the halls and public areas make a favorable impression?	☐	☐
2. Are the carpets reasonably intact and attractive?	☐	☐
3. Are the draperies in good shape and attractive?	☐	☐
4. Is there evidence of a nice decorative touch (pictures, plants)?	☐	☐
5. Are the premises neat and orderly?	☐	☐
6. Are the grounds well-groomed and attractive?	☐	☐
7. Are there attractive accents outdoors (shrubs, flowers, trees)?	☐	☐
8. Are the fixtures acceptable and operable?	☐	☐
9. Is the condition of the paint (inside and out) acceptable?	☐	☐
10. Are the appliances in good order?	☐	☐
11. Other points (you add) _____	☐	☐

B. AREAS WHERE STRUCTURAL DEFECTS AND MAJOR DEFICIENCIES COULD BE VERY COSTLY. BEWARE!

	Needs Improvement	
	Yes	No
1. Is the building structure (foundation, major walls) free of suspicious cracks and breaks?	☐	☐
2. Is the basement free of evidence of water problems (musty smell, mold, puddling, moisture where walls and floor meet, stains)?	☐	☐
3. Is the plumbing modern and in acceptable condition?	☐	☐

4.	Is the heating and air-conditioning system in good operating order?	☐	☐
5.	Is the electrical wiring up to code and adequate?	☐	☐
6.	Is the property free of termites or other insect infestation?	☐	☐
7.	Is the roof in good condition?	☐	☐
8.	Is there adequate parking?	☐	☐
9.	Does the property meet all local building codes?	☐	☐
10.	Are existing facilities adequate for rental needs or will additions be necessary?	☐	☐
11.	Others (you add) _____	☐	☐

C. SOME TIPS ON IMPROVEMENTS

1. Don't be too concerned with minor, cosmetic needs—these can be corrected relatively cheaply and enhance the attractiveness and resale value of the property.

2. Don't overimprove—let the most attractive competing property in the neighborhood establish a kind of upper limit. The rents probably cannot be raised much beyond the competitor's rent.

3. Tenants can often be engaged for minor repairs in return for consideration with their rent.

4. Use professional building appraisers and inspectors to accomplish the major structural checks—it's good insurance.

5. Read widely in the literature on property structure analysis. A good source is *How I Turned $1,000 into Five Million in Real Estate in My Spare Time,* Revised Edition, by William Nickerson (1980).

D. PUTTING THE PROFESSIONALS ON YOUR SIDE

Finally, as we close this group of sections on analysis, it is well to pause and reconsider the numerous professionals we have needed to use. The chart below will bring many of them to mind.

How have these professionals played a vital role in the process of real estate investment?

Putting the Professionals on Your Side



- Title Companies (In Canada: provincial and municipal sources)
  —The listing package
  —Courthouse training
- Management Companies
- Lawyers
- Accountants
- Bank Loan Officers
- Property Rental Companies
- Building Inspectors
- Insurance Agents
- Appraisers

E. REAL ESTATE AGENTS

The selection of a real estate professional to work with is a crucial matter. The majority of real estate agents do *not* understand the creative financing, single agency (buyer's broker) exchanging, and estate-building techniques taught in this seminar. How can you locate a knowledgeable and competent real estate person to work with? Here are four ideas to consider:

(1) Turn to the ACRE Chapter in your area or the area in which you are buying. Most "Nothing Down" Seminar groups contain a number of real estate agents, brokers, and agents who are knowledgeable about creative financing techniques. You can contact them at the monthly meetings or through the local ACRE president.

(2) The Society of Exchange Counselors. Many of the creative real estate techniques used today were originated and perfected by members of the S.E.C. during the 1960s. Within their fairly select membership are some of the most creative real estate practitioners. They tend to work on larger real estate transactions and are knowledgeable in the use of exchanging as a creative marketing tool as well as tax deferral techniques.

c/o Society of Exchange Counselors
P.O. Box 41964
Sacramento, CA 95841
(916) 920-4031

(3) *Who's Who in Creative Real Estate.* Many lawyers and accountants are not familiar with the legal and tax-related intricacies of real estate transactions. It is important to locate real-estate-oriented legal and tax counsel. To assist in this endeavor, the publishers of the national directory Who's Who in Creative Real Estate have a special section for real estate oriented attorneys and C.P.A.s.

The individuals listed in the directory have invested considerable time, effort, and expense to educate themselves above and beyond the minimum real estate licensing standards. These individuals possess an overview of real estate unknown and unheard of by the average real estate licensee. To obtain a directory, send $25.00 (plus 6 percent tax if you live in California) to:

Who's Who in Creative Real Estate
921 E. Main Street, Suite F
Ventura, CA 93001
(805) 648-3109

Graduates of the "Nothing Down" Seminar should also turn to their monthly ACRE Chapter for leads and references to reputable real-estate-oriented attorneys and accountants whose services they could retain.

(4) Certified Commercial Investment Member. Another group of nationally recognized real estate agents who are trained and have demonstrated ability in the field of Commercial and Investment Real Estate have

the designation of CCIM, Certified Commercial Investment Member of the Realtors National Marketing Institute, (a similar certification is offered to qualifying professionals by the Canadian Real Estate Association).

How have these professionals played a vital role in the process of real estate investment? For more information write to:

The National Association of Realtors
430 N. Michigan Avenue
Chicago, IL 60611
(312) 440-8000

In Canada, check your local board of Realtors for up-to-date information.

When you need guidance and expertise in real estate investments, try to locate one of the trained specialists mentioned herein for assistance. It should substantially improve your chances of a well-designed, financially successful transaction.

A Final Note on Buyer's Brokers. One of the best ways to put a real estate professional on your side is to hire a broker to represent you and pay him a fee.

It is common for sellers of real property to employ a broker to list and sell their property. Where Multiple Listing Services are involved, other members of MLS (cooperating brokers) are usually subagents of the seller. If a buyer wants professional client representation, then he should hire a broker to represent him and pay his fee.

It should also be noted that property owners often need input on their real estate affairs in circumstances where there may not be any buying, selling, or exchanging of property in the near future. Appropriate information can be obtained from knowledgeable real estate agents who provide this information on a consulting basis. They may charge an hourly rate or a flat fee for this type of service. See *Nothing Down,* New Revised Edition (Simon and Schuster, 1984), pp. 39–99 for more information on using buyer's brokers.

F. THE NOTHING DOWN PROPERTY SELECTION MATRIX

We conclude this section with one of the most important investment tools in the entire Nothing Down Program: The "Nothing Down Property Selection Matrix" on the next page. In the previous five sections, we have provided the essential information for analyzing a property on the basis of the seller's flexibility, the location of the property, the financial situation, the market situation (price level), and the property structure. The decision matrix on the next two pages enables the buyer to apply this information to a given property and make an informed decision about whether or not to buy.

The decision "Yea" or "Nay" on a given property is not something to take lightly or make with the flip of a coin. While the decision matrix is not intended to be an automatic guarantee of success, it does at least provide a rational framework for the process of selecting properties. All the important elements of analysis are brought together as a safety check on the investor's "gut feel" for the situation at hand.

This version of the "Property Selection Grid" is from Robert G. Allen's *Creating Wealth* (New York: Simon and Schuster, 1984), p. 112.

PROPERTY SELECTION GRID

	POOR	AVERAGE	EXCELLENT
1 SELLER'S MOTIVATION AND FLEXIBILITY	**1 POINT** Won't budge on price or terms. "Take it or leave it." Doesn't need to sell. Not anxious at all. In the driver's seat.	**2 POINTS** Might consider a small discount in price. Needs cash for new house or property. Needs cash for bills, etc. May carry small second or contract but leery of unusual deals.	**3 POINTS** Needs cash for pressing items, i.e. behind in payments, etc. Or, doesn't need cash at all . . . has tax, management, transfer, time problems, or divorce, retiree, or investor looking for a solution without major need for cash. Flexible in price or terms.
2 LOCATION	**0 NEVER** No pride of ownership. Junk and debris in streets. High crime. No appealing shopping close by. Abandoned buildings and boarded-up properties. Close to major streets, industrial areas, or commercial zones (across the street). Far from employment centers or commuter accessibility.	**2 POINTS** May be clean, older neighborhoods. Close to shopping, churches, schools, etc., but not very appealing. Working class tenants, neat, established. May be poor location on the upswing with pioneer fixer-uppers. Nicer inner-city neighborhoods.	**3 POINTS** Easy accessibility to all necessary amenities and transportation. Middle-class, suburban neighborhoods. Not on busy streets; cul-de-sacs ideal. Properties nearby very similar in price. Good foliage and landscaping except in brand new subdivisions. Only high-class inner-city locations.
3 FINANCING	**1 POINT** More than 15% down. Seller needs lots of cash and wants all of his equity. Or, property will have heavy negative cash flows for more than three years from date of purchase. **Consider only if price is excellent.**	**2 POINTS** Financing required from an institution with up to 15% down of buyer's money. Credit checks, Institutional, secured loans for part of the down payment (high interest, high monthly payments). Seller carries small amounts. Cash required from buyer. Balloons due in less than 5 years.	**3 POINTS** Less than 5% of buyer cash involved. Seller carries most of the financing at lower than market rates with no balloons in less than 7 years. No negative cash flows projected beyond the first year. Contract sale, no credit checks.
4 PRICE	**1 POINT** 10% or more above the reasonable market price. **Consider only if financing is excellent.**	**2 POINTS** Within + or − 5% of market price.	**3 POINTS** At least 10% or more below market price.
5 PROPERTY CONDITION	**1 POINT** **Consider only if price is excellent.** Needs major cosmetic and structural improvements. At least 10% of purchase price will need to be spent immediately to make unit rentable. Improvements do not significantly improve the rent roll because of quality of tenants and location. Improvements not to increase value more than 10% above purchase price. Usually associated with poor locations. Possible to find this property in excellent locations where prices are so high than improvements do not increase value but just make units acceptable to renters. Viewed as making a larger down payment (for improvements) and receiving an average-priced property.	**2 POINTS** This is the true fixer-upper! Cosmetic improvements would be nice but not immediately necessary. Costs not to exceed 5% of the purchase price. Cosmetic improvements immediately affect the value upwards and make the property more desirable, saleable, and attractive. Not much structural work (if any) is necessary . . . only paint, landscaping, drapes, and other inexpensive improvements. This type of property should not be bought if the buyer does not have the time or mental capacity to undertake supervision of improvements. This property can prove to be the most profitable in the short run. The worst house in the best neighborhood.	**3 POINTS** Newer property or older property with recent renovation. No problems, clean inside and out . . . good landscaping. New components to replace major items. May have been a recent fixer-upper project which is being sold by a don't wanter at an excellent price. No work necessary before renter moves in. Solid property with a hassle factor of zero. Quick closing, quick rent-up, quick cash flow.

- Analyze and assign a point value to each factor of a property.
- If in doubt about a point value always pick the lower number.
- Add up the numbers and total.
- The lowest acceptable score is 9, the highest possible is 15.
- Greater fools always buy property in the 9, 10, 11 range.
- Great investors always buy property in the 12, 13, 14, 15 range.

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TOTAL SCORE

The Ten Commandments of Property Selection

1. Never buy a property in a poor location—not under any circumstances!
2. Never buy a property with a point total less than nine!
3. Never buy a property with poor financing unless it has an excellent price!
4. Never buy a property with a poor price unless it has excellent financing!
5. Never buy a property in poor condition unless it has an excellent price and you have the capital, know-how (can be hired), and mental toughness to want to improve a property!
6. Never buy a property unless it has one excellent factor (score of three).
7. Don't live the greater fool theory. Stay as far from the line as possible. A nine is a marginal property. The higher the score, the more desirable the property. Don't buy only for tax shelter. Most tax shelters are nines.
8. Never borrow partnership money to invest in a marginal property.
9. Never buy a property that has more than two poor factors (points = 1) unless under the extremely rare circumstance of an immediate condo conversion planned to take place after the purchase.
10. Never buy a property unless you are committed to *following through* on the major and minor details of property management, whether you handle the management or hire a professional company.

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SECTION K

Creative Structuring Of Paper

Robert G. Allen

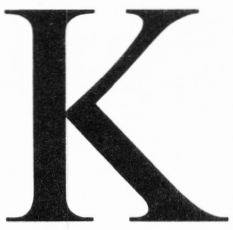
M.B.A.

IN COOPERATION WITH

Richard J. Allen

Ph.D

Creative Structuring of Paper: Dealing with Negative Cash Flows



A. THE EFFECTIVE USE OF "PAPER" IN CREATIVE FINANCING ..... K- 3
1. Putting Time on Your Side ..... K- 3
2. Test Yourself with This Problem ..... K- 3
3. Ways of Caging That Pet Alligator ..... K- 4
B. CREATIVE PAPER: EIGHT TECHNIQUES FOR DEALING WITH NEGATIVE CASH FLOW ..... K- 5
Technique 1: The Straight Balloon Mortgage ..... K- 5
Technique 2: Reverse Paper ..... K- 5
Technique 3: Pay Interest Only ..... K- 5
Technique 4: Increase the Length of Amortization with a Balloon Payment ..... K- 5
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Technique 7: Moratorium on Payments until Cash Flow Increases ..... K- 6
Technique 8: Structure the Seller's Note to Seasonal Demands ..... K- 6
C. ADDITIONAL STRATEGIES USING PARTNERS ..... K- 6
D. WHAT TO DO ABOUT BALLOON NOTES ..... K- 7

Creative Structuring of Paper: Dealing with Negative Cash Flows

K

A. THE EFFECTIVE USE OF "PAPER" IN CREATIVE FINANCING

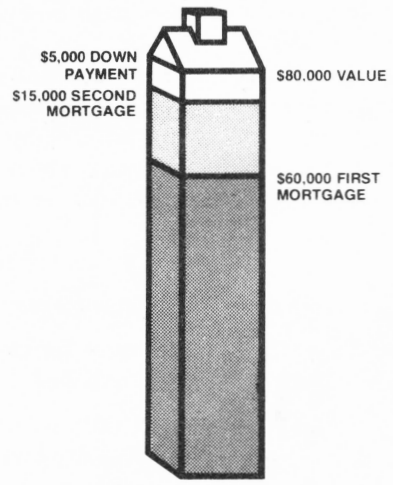
1. Putting Time on Your Side

The key to borrowing money and making good use of paper is to incur debt by deferring the obligation to repay as far into the future as possible. This puts time on your side. In fact, the word "TIME" is a key word summarizing the four rules of making the best use of paper, as for example in the case of notes:

(1) **T** Term of repayment should be as long as possible.
(2) **I** Interest rate should be as low as possible.
(3) **M** Monthly payments either nil or as low as possible.
(4) **E** Equity or property used as collateral—little or none at all.

Using paper to your benefit is critical to the success of any investment.

2. Test Yourself with this Problem



3-UNIT APARTMENT BUILDING

The following statements quickly summarize the important facts of the purchase illustrated above:

1. The buyer has borrowed $5,000 from his credit union with a six-month note at 11 percent interest.

2. His first mortgage loan is payable over 25 years at $550 per month.

3. The seller has taken back a second mortgage for the balance of his equity ($15,000), payable over seven years with monthly payments of $250, including 10 percent interest (a very good rate).

4. The buyer has only $100 extra per month personal cash flow to invest.

5. The seller had told the buyer that rents were $350 from each of the three units and that expenses should average $200 per month.

6. After the purchase, the buyer discovers that rents are really $300 per month for two of the units and $325 for the third, and that expenses were $400 per month from October through March and $200 per month from April through September.

7. The buyer took possession in December. Here's what happened in January:

Monthly gross rents	$925
January expense	$400
First mortgage payment	$550
Second mortgage payment	$250

Question: Will this investor be eaten alive by his pet alligator?

Your Comments:

_____

_____

_____

_____

_____

_____

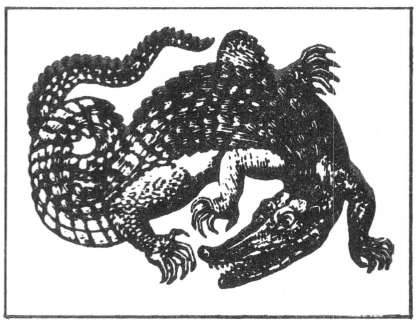
3. Ways of Caging That Pet Alligator

The strategies for dealing with a negative cash flow are summarized in the illustration with the key word "CAGES."

Since adjustments in rents and expenses are the only strategies normally available after the purchase is completed, the buyer must do his homework and exercise great ingenuity in the other pre-closing strategies.

Note in particular what the buyer of the above three-unit apartment building could have done with creative structuring of "paper."

ALLIGATOR CAGES



Alligator Cages

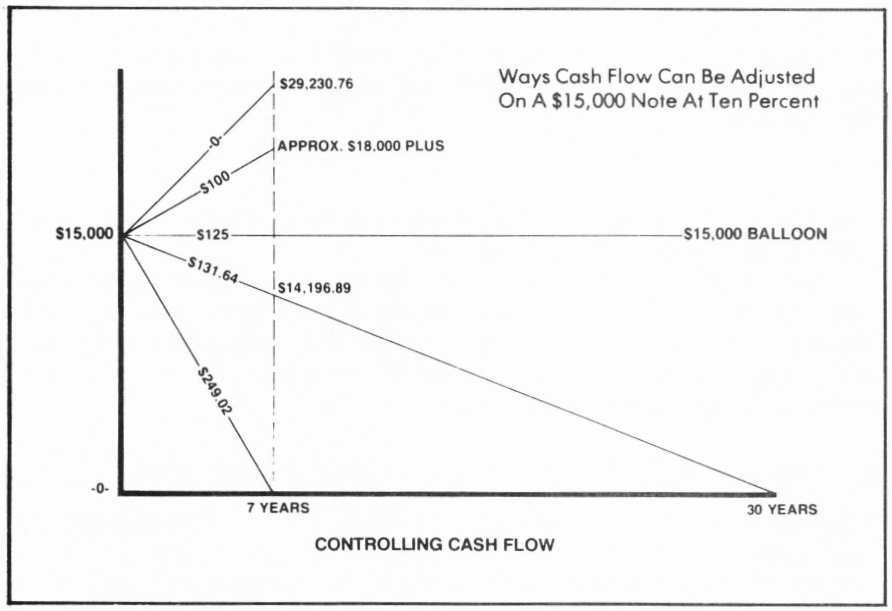
Strategies for caging the alligator (negative cash flow):

- **C** Cut the seller's price
- **A** Ask for more rent
- **G** Give more toward down payment
- **E** Eliminate more expenses
- **S** Structure the mortgage payments

B. CREATIVE PAPER: EIGHT TECHNIQUES FOR DEALING WITH NEGATIVE CASH FLOW (SEE CHART)

Technique 1: The Straight Balloon Mortgage

In this case, there are no monthly payments. The full amount is paid in a lump sum at the end of a specified time. Using the illustration mentioned earlier, the buyer could have offered the seller a $15,000 mortgage secured against the property and due in seven years when it would be worth $29,230.76. Naturally the buyer must prepare for the time when the balloon comes due by investing extra cash flow in ways that will generate funds for the payoff. There is also the possibility that the property will not appreciate as much as planned or that economic conditions will generate a tight money market at the time the balloon falls due. The buyer should have contingencies in place for this eventuality. For example, it would be prudent to negotiate a roll-over provision allowing the buyer to extend the balloon an additional year (usually with a paydown of the principal by a specified amount or some other "sweetener").



Technique 2: Reverse Paper

In this variation, a lesser amount is paid each month, with a balloon for the balance at the end of a specified period. The monthly payment may not even cover the interest, hence the term "reverse" paper or "walking the paper backwards." Thus in our example the buyer may pay only, say, $100 per month of the $250 required to amortize the $15,000 note in seven years. The $150 difference is then added to the principal of the note. The note will continue to grow slowly over time, and it must, of course, be paid off later.

Technique 3: Pay Interest Only

Rather than amortizing the loan, negotiate a semi-annual or annual interest-only payment. This gives you time to obtain the needed money. In our example, the buyer might pay $750 twice a year or $1,500 annually. Meanwhile, the buyer has time to secure the needed funds to pay off the principal.

Technique 4: Increase the Length of Amortization with a Balloon Payment

The note is paid back using monthly installments as if it were structured to be paid back over 25 or 30 years. However, after a specified time, the balance is paid in a lump sum. In the illustration above, the buyer could have structured the mortgage for a 30-year amortization at $131.64 per month,

then paid the balance of $14,196.89 at the end of seven years. (See chart for variations on amortization of the note.)

Technique 5: Convert Any Balloons to Amortizing Notes When They Are Due

In our illustration, the $5,000 six-month note from the credit union could have been converted to an amortizing loan at 12 percent with a pay-back period of five years (monthly payments of $111.12). Meanwhile, rents could have been raised to make up the added monthly burden.

Technique 6: Increase the Interest Rate Gradually

The $15,000 note in the illustration was set at 10 percent. Perhaps the seller would have accepted 6 percent the first year, with a one point increase each year until 10 percent was being paid in the balance. This way payments could start lower and escalate with your ability to pay. Perhaps as an inducement the buyer could even permit the interest note to climb to 11 percent or 12 percent at the end of the climb.

Technique 7: Moratorium on Payments until Cash Flow Increases

For example, the buyer in our example could have negotiated a two-year delay in payments until he could have raised the rents high enough to cover the expenses.

Technique 8: Structure the Seller's Note to Seasonal Demands

Payments could be adjusted downward in periods of heavy expenses and upwards in periods of lighter expenses.

Always try to negotiate your paper with the seller to give you at least one year's breathing room before full amortized payments begin. Keep your negative cash flows to a minimum for the first year, which is the most difficult time for the beginning investor. This will give you time to raise the rents and bring expenses into line.

C. ADDITIONAL STRATEGIES USING PARTNERS

When a buyer is faced with a negative cash flow situation, there are only four basic options:

(1) Pay it—this may be tolerable if not too expensive, especially where little or no money is put down. After all, it may be wise for tax purposes to invest this way rather than pay higher income taxes.

(2) Structure the financing to cure or reduce the negative—as in the eight preceding techniques.

(3) Have someone else pay it.

(4) Pass up the deal altogether and keep looking for better opportunities.

Frequently the deal is so promising that the buyer is reluctant to pass it up, even though he is unable to cure the negative cash flow alone. He may consider bringing someone else in on the deal to take care of the negatives in exchange for certain benefits, usually an equity position in the property (see Item I of Section O for partnership techniques No. 44 and No. 45). Bringing in a partner is an expensive way to go; however, a part of the pie is better than no pie at all. In times of high interest rates and tight money, the partnership solution to potential negative cash flows is a strategy to keep in mind.

A variation of this approach is "tenant equity participation," where the tenant pays all debt service (even though it may be considerably higher than the market rent level) plus all expenses. In exchange for taking care of the negative cash flow in this way, the tenant is given part ownership in the property. Competent legal expertise is critical in drawing up such agreements. The tenant/equity participant will, of course, have to satisfy the terms of the agreement according to specific criteria and time requirements, after

which time one party will buy the other out or the property will be sold and the proceeds divided as originally agreed upon.

The tenant equity participation arrangements of this type—where the tenant is deeded part ownership of a property—are fairly recent and not yet thoroughly tested in the courts. What happens if a tenant fails to pay the agreed-on amounts as required, and the investor/owner has to take steps to terminate the agreement and take back a full equity position? The outcome seems fairly straight-forward—"No pay, no equity." But the tenant may sue after having paid in a considerable sum of money, and there may be unforeseen legal ramifications. Expert help is essential in such arrangements from the outset.

Other tenant-partnership arrangements are possible. An example is the lease-option agreement where the tenant pays higher-than-market rents in order to secure the privilege of being able to buy the property at a specified price within a specified period of time. The tenant takes care of all the negative cash flow, and the investor/seller builds on acceptable profit into the arrangement. There are many other variations.

D. WHAT TO DO ABOUT BALLOON NOTES

Beginning investors will often succumb to the easy solution of agreeing to give the seller a short-fuse single-payment note in exchange for early relief from negative cash flows. Let's be clear about it—*balloons can be dangerous!* Anything less than a five or seven year term on a balloon is too short-fused in these times of uncertain growth and high interest rates. Be sure you can satisfy the terms of a balloon note before agreeing to them. The offer to purchase involving a balloon should always contain a clause where the seller must permit the buyer to extend the balloon for an additional year (or longer) provided a sweetener is used (usually a one-time payment toward principal or an increase in the interest rate on the remaining principal).

What does the investor do when the balloon note comes due? There are seven basic strategies.

(1) Refinance the property. If possible, pull out enough money to pay off the balloon and still have an extra fund for servicing negative cash flows.

(2) Refinance another property to generate the needed funds.

(3) Renegotiate the balloon. Perhaps the seller would convert the balloon to monthly payments and/or postpone the payment of the balance until a later date. Usually a bonus is required—a hike in the interest, pay-down of part of the principal, or higher monthly payments beginning some time before the balloon is due. Above all, don't wait until a month before the balloon is due to renegotiate it—start at least a year ahead of time, preferably two!

(4) Bring in a partner to pay the balloon—either as an investment to be repaid or in exchange for an equity position in the property.

(5) Sell the property—pay off the balloon and take your profit. (In tough money times it may be necessary to sell for nothing down and discount the carry back note to raise the needed capital.)

(6) Sell another property in your portfolio.

(7) If all else fails, give the property back to the seller. (At least you will have had the tax advantages and perhaps some cash flow in the meantime!)

Be careful with balloons!

Creating Wealth

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Manual

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SECTION L

How To Negotiate

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How to Negotiate

L

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How to Negotiate



A. TIMING: WHEN DOES THE NEGOTIATION BEGIN?

In the initial contact with the seller, our objectives were three-fold: first, to determine how flexible the seller would be; second, to gather information about the desirability of the property; and third, to build up the seller's trust.

Genuine negotiation begins when it is clear that we are dealing with a flexible don't wanter and when the initial analysis has satisfied us that the property is truly of interest to us.

B. THE TONE OF THE NEGOTIATION

1. The Five Ps of Interaction

The same assumptions and attitudes that governed the seller analysis also pertain to the negotiation, i.e., the buyer should:

(1) Put the **P**erson before the **P**roperty (cultivate a genuine interest in the seller as a person).

(2) Assume the role of **P**roblem-solver.

(3) Ask **P**enetrating but **P**olite questions.

(4) **P**ace it slowly.

(5) **P**ersistence pays off.

2. A Game with a Win/Win Outcome

The difference now is that the interaction game is moving into the final inning, and the specifics of the deal will need to be pinned down. Without compromising any of the human relations values espoused by the "Nothing Down" philosophy, the buyer needs to apply in the negotiation process all the skills at his disposal for striking the best bargains. He needs to be as "wise as a serpent" and as "harmless as a dove" (Matthew 10:16). Another way of saying the same thing is this: the buyer wants to assure a win/win outcome to the game. Because of his creative approach, the buyer will solve the don't wanter's problem and also acquire a good investment property for "Nothing Down." That's the effective non-use of cash!

C. FIVE KEY RULES FOR THE NEGOTIATING GAME

1. Pitch Only at the Don't Wanter

The cornerstone of the "Nothing Down" system is the strategy of concentrating your efforts where they will do the most good: on the flexible seller. If it becomes clear in the negotiation that the seller is less flexible than you had anticipated, it may be necessary to "call off the game" and move on. Precise, penetrating questions will quickly bring out the degree of flexibility of the seller. (As noted in Section O, the pitch can also work with private parties who are holders of underlying mortgages.)

2. Interchange of Price/Terms Advantage

In the ideal situation, the buyer would be able to set both the price and the terms for the deal: a shutout! In practice, however, both parties win: one sets the price; one sets the terms. The rule is:

"You pick the price; I'll pick the terms."
"You pick the terms; I'll pick the price."

In some cases it might even be to your advantage to offer a *higher* price than the seller is asking so that you can get better terms (e.g., nothing down).

a. Five Flexibilities in the Negotiation Process. There are five major flexibilities in the negotiation process:

(1) Price
(2) Interest rate
(3) Monthly payments
(4) Down payment
(5) Closing date

Which are the most important?

3. Temper High Profit Expectations

Without being rude or negative, it is possible to convey to the seller your awareness of flaws in the building. For example, you can pause at problem spots (leaky faucets, discolored counter tops, evidence of moisture in the basement, etc.) and jot down notes in a notepad. In addition, you can remain fairly neutral and unemotional about the property and even toss in casual references about the competition (similar properties you are considering). Act the part of the "don't wanter buyer." The person who cares least (i.e, has the least emotional involvement) will control the situation.

4. Concentrate on Relieving the Seller's Fears

It is essential that you respond to the true reasons for the seller's wanting to dispose of the property. Learn what his fears and problems are and then help him solve the problem. Keep before you the 20 don't wanter conditions reviewed earlier.

5. Homework

Do your homework. Know ahead of time how far you are prepared to go in the negotiation. Decide beforehand the benefits you want. Pick the limits for price, terms, down payment, monthly payments, etc., beyond which you will not bend. Get up and walk out graciously when you see that you are not getting what you want.

6. Key Word for the Negotiating Game: PITCH

P	Pitch to Don't Wanters
I	Interchange Price/Terms Advantages
T	Tear Down High Profit Expectation
C	Concentrate on Relieving the Seller's Fears
H	Homework

D. THREE ADDITIONAL STRATEGIES FOR NEGOTIATING

1. Simplicity

Keep it simple (KISS). Avoid real estate jargon that will be distracting and confusing to the seller. "A confused mind always says 'No.'" A few examples follow:

Jargon	Simplicity
"Would you accept a substitution of collateral?"	"Would you be willing to secure the second mortgage against my four-plex over on Center Street?"

"How about a second mortgage crank on your property?"	"Would you be willing to take back a second mortgage for a portion of your equity? I could give you a down payment of $5,000 and the remainder of your equity in cash by refinancing the property."
"Would you be amenable to a wrap-around mortgage?"	"I could give you a contract covering the underlying first mortgage and the balance of your equity. What would you think of 10 percent interest for the whole contract?"

2. Silence

"The first person to mention a number loses." Don't be too hasty about pinning yourself down to a specific figure. React to any of the seller's proposals with, "I might be interested in that" or "Hmmm, let me think about that as I look over the building once more."

3. Solitude

Unless you have a deal you can't refuse, go away after the negotiations to ponder your position and write out your offer.

E. THE NEGOTIATION CHECKLIST

Let's suppose we have a $50,000 house that has $15,000 equity. As part of our financial statement, we also have an $80,000 house that we're living in with a $65,000 mortgage and a $15,000 equity, and we also own a $5,000 motor boat that we own free and clear that we don't want. So let's start with the negotiation checklist.

The buyer starts the negotiation process at the bottom of the list from a "no cash" position. The seller will normally take a stand at the top of the list where his equity can be fully cashed out.

Seller's starting point	Cash	No cash involved	Buyer's starting point

1. Hard cold cash to existing mortgage
2. Cash down payment and refinance
3. Cash down payment with seller carrying back second mortgage or a contract
4. Cash plus equity in other property
5. Cash plus mortgage on other property
6. Equity in other property
7. Equity plus mortgage on purchased property
8. Equity mortgage on other property
9. Mortgage on purchased property
10. Mortgage on other property
11. Unsecured paper (note) for entire equity

Low seller motivation (prices lower)	High seller motivation (prices higher)	Lowest prices	Highest prices

Then the compromising begins. Note the dynamics of motivation: from the standpoint of the selling price, liberal terms (low in the chart) will tend to support a high price; hence, the seller will be highly motivated. Strict terms (high in the chart) will tend to drive the price downward, and the seller may be less motivated to sell. Somewhere between these two extremes, he will be motivated to compromise and come to terms.

As far as the example goes, we start on number eleven, since we are starting at the bottom, and we offer the seller a $15,000 unsecured loan. Will people accept unsecured notes for at least a part of their equity? Well, I've only been able to do it three or four times in the past few years. Generally, people don't like to accept unsecured notes, but sometimes they find themselves in situations where they find they have to, or they find themselves in situations where they don't ask for a secured note. Sometimes they don't understand that they are supposed to have a secured loan.

One of our graduates found a fellow who was selling a home and had about a $15,000 equity in it. By asking the seller first for an unsecured loan, he was able to buy the property from him by just using his own signature by giving the fellow a $15,000 unsecured note. Then he went and sold the house and collected the $15,000 in cash and used that as his initial seed money to start his investment program. You remember that the unsecured note means that if you don't pay the loan off, the holder of the note can sell or attach everything you own until that note is paid off. So it has its benefits, and it has its detriments. You never can know if the person will accept that unless you ask. And this is my challenge to you.

Suppose he doesn't accept your $15,000 unsecured note. Then you go up to number 10 in the checklist, which is a mortgage on other property. "In other words, Mr. Seller, as an entire down payment on your $50,000 house, would you accept as payment for your equity a $15,000 note secured against my own personal residence?" If he doesn't accept that, he might go to number nine. "Would you then accept a $15,000 second mortgage loan secured against your own property?" And on one of those transactions (numbers 9, 10, or 11) I am able to get in with absolutely no cash involved.

You go on to number eight; he says perhaps he won't accept that. You say, "Well, then will you take my $5,000 boat plus the mortgage on my house for $10,000?" Therefore, the seller is getting something of value and also receives a note for payment. If he won't accept that, we go to number seven, which is: "Accept my $5,000 boat and a $10,000 note on your property." If he won't accept that, then you say, "All right, then we'll go to number six. Will you accept my $5,000 boat and my $10,000 recreational lot that's located in XYZ county?" You're always trying to be able to have the seller accept what you have without having to use your cash. Let's go to number five. In this area we are starting to have cash involved.

"Will you accept a $5,000 cash payment plus a $10,000 mortgage on my house?" If not, then number four. "Will you accept a $5,000 cash payment plus equity in my recreational lot at $10,000? Therefore, you are getting $5,000 in cash plus some equity that you can use for something else. If not, would you accept a $5,000 down payment in cash with a $10,000 note second mortgage or a contract on your own property? If not, will you let me go and refinance your property for $45,000 and give you the $10,000 in cash for the refinance plus a $5,000 down payment?" And number one is, "Do you have to have your $15,000 in cash? If so, I don't think I'm interested."

As I move from the bottom of this chart to the top of this chart, I'm negotiating for lower prices. As I move from the top of this chart to the bottom of this chart, I'm expecting to pay higher prices. The reason that I have this chart for your inspection is so that you can get in the habit of

starting at the bottom and moving up instead of starting at the top where the seller wants you and moving down. You will find that you will be able to use this chart very accurately if you can locate a don't wanter. The less a person is flexible the more you know he is going to require that you start at the top of the list.

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SECTION M

How To Make Written Offers That Protect The Buyer

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How to Make Written Offers That Protect the Buyer

M

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How to Make Written Offers That Protect the Buyer

M

A. THE EARNEST MONEY RECEIPT AND OFFER TO PURCHASE

In most states of the Union and in most provinces of Canada, negotiations become legally binding when both buyer and seller have signed a written agreement called the Earnest Money Receipt (also know as the Offer to Purchase, Purchase Money Receipt, or Deposit Receipt). In Canada, the document is commonly referred to as the "Interim Agreement" or "Offer to Purchase" or "Interim Sales Agreement." By signing the form and making a cash deposit, the buyer indicates his earnestness to buy the property; by signing the form and receipting the deposit, the seller indicates that he accepts the offer to purchase, together with the conditions for following through with the purchase as described herein. If the buyer defaults, the seller can keep the cash deposit as liquidated damages. The Earnest Money Agreement ties up the property for a short period of time and is therefore really a very short-term option to purchase.

B. GUIDELINES THAT WILL PROTECT YOU

It is critical that you observe the following protective guidelines in filling out the Offer to Purchase:

1. Name of the Purchaser

This should always read "John Doe (your name) and/or his assigns" everywhere it is called for in the document. You might decide to "sell" the property to another "buyer" at closing and make a profit. The new buyer can qualify as your "assigns." Later on in the seminar we'll discuss this technique, called the "Earnest Money Option," in more detail.

2. Amount of Deposit

The laws in most states and in some provinces state that $1.00 is legal and binding. Most sellers will require at least $500. The idea is to put down as little as possible. I like to use $100. This limits your liability in case you decide not to go through with the offer for some reason. *Be sure to indicate that the deposit will constitute the entire liquidated damages in case of default.* (See below under "Some Additional Tips for Reducing Risk.")

If the real estate agent objects to such a small deposit (as he should if he is a good agent), you may suggest that you make many offers to purchase real estate in the course of one month and you don't like to tie up your funds in the trust accounts of real estate companies because it limits your ability to make future offers. If the seller requires additional deposit, it might be arranged if the price and terms are right. Always maintain a policy of small deposits unless you feel that you might lose an excellent buy by offending the seller. If you don't have the cash for a large deposit, you may consider giving the seller a personal note (or irrevocable letter of credit) made negotiable at closing. Such an arrangement may seem to the seller almost like cash.

3. Who Holds the Deposit?

If a real estate agent is involved, the agency will hold the funds in a trust

account until all the terms and conditions of the agreement are fulfilled. If no real estate agent is involved, the funds can be held in trust by a third party, preferably a title company or a lawyer. It is best to avoid giving the funds to the seller directly.

4. The Closing Date

Leave yourself enough flexibility to raise needed capital for the down payment, to search for a partner, or to "sell" the property to another person (your assigns) for a higher price. Leave at least four weeks to close and longer if conventional financing is sought. You would only close sooner if it could be to your advantage.

If you are buying a rental unit, arrange to close on the day the rents are due. These funds will belong to you as the new owner. In most areas they can be used as part of the down payment. However, be sure to check on local laws and practices in this regard.

5. The "Subject To" Clause

These clauses, sometimes (though not always accurately) known as weasel clauses, are inserted in the Earnest Money Agreement to limit your liability even further. Examples are these:

(a) Subject to an inspection by my partner within three days of the seller's acceptance of the offer. (If you decide you don't want the property, have someone inspect the property and write a letter of disapproval.)

(b) Subject to all appliances, heaters, refrigerators, stoves, air conditioners, and all other equipment pertaining to the operation of the property being in good working order as of the day of the closing.

(c) Subject to termite inspection, building code inspection, or roofing, plumbing, structural checks, or any other checks you deem necessary.

(d) Subject to minor or major repairs being done by the seller according to your negotiations.

(e) Subject to obtaining suitable and adequate financing. Spell it out in detail as to terms and interest rate.

(f) Subject to inspection of the financial records.

(g) Subject to clear and marketable title or survey if necessary.

(h) Subject to approval from planning bodies (if additional development is contemplated as part of the value of purchase).

(i) Subject to satisfactory inspection of any tenant contracts and service agreements which go with the title(s).

6. Further Conditions

Additional items that might be included in the agreement according to negotiations:

(a) Seller to pay points (for example, with government-insured loans).

(b) Seller to relinquish to the buyer all the tax and insurance impounds as part of the purchase price.

(c) Seller to pay all the closing costs.

C. THE COUNTER OFFER

The seller will likely respond to your offer with a counter offer. The real estate agent (if any) can be the go-between in this final round of negotiation. Make sure that the seller understands that the theme of this phase is "Don't tell me what you won't do; tell me what you will do." Insist that since you were courteous enough to make a formal, written offer, he should be courteous enough to respond in writing.

D. MAKE MANY OFFERS

It is a numbers game! Make frequent offers on many properties. Research

with the Nothing Down graduates has indicated that it takes approximately five offers to achieve a good creative deal, and 10 offers to achieve a true "nothing down" deal.

E. SOME ADDITIONAL TIPS FOR REDUCING RISK

Always get expert legal and accounting advice in preparing offers to purchase. The following kinds of clauses will help reduce risk for the buyer. They may be adapted for use in particular situations:

(a) The right to substitute collateral on a note: "Buyer has the right to substitute collateral of equal or greater value on the second mortgage (second trust deed, etc.) at any time, with the Seller having the right to approve."

(b) The right to extend a balloon payment: "Buyer shall have the right to extend the balloon payment, at his option, for an additional twelve months, provided a principal payment of $_____ is made to the Seller on the original due date of the balloon."

(c) The right to prepay a loan without penalty: "Buyer may at any time and without penalty pay in full all amounts owing to the Seller under conditions and terms of this agreement."

(d) First right of refusal on an owner carry back: "This arrangement is contingent upon Buyer having first right of refusal on the second note and deed of trust (etc.) if Seller should decide to sell the note."

(e) Limitation on damages: " In the event the Buyer fails to complete the purchase as herein provided, the earnest money deposit shall be retained by the Seller as total and entire liquidated damages."

(f) Limitation on liability: "The liability on the part of the Buyer to satisfy the terms and condi,tions of the note(s) executed in favor of the Seller as part of this agreement shall be limited to the property securing such note(s) and shall not extend beyond this. (Liability of this contract shall be limited to the property itself and not extend beyond this.)"

(g) Miscellaneous examples: "Seller agrees to deliver the premises in a clean and orderly condition at the time of closing. Seller agrees to have all utilities paid in full to date of closing."

There are many other provisions for reducing the buyer's risk. Consult with a competent real estate attorney for details of the documentation.

Note: Included below is a sample "Earnest Money Receipt and Offer to Purchase" that contains the phraseology of use to a creative buyer.

Earnest Money Receipt and Offer to Purchase

"This is a legally-binding contract; if not understood, seek competent advice."

SAMPLE

1. Date and Place of Offer: _____ 19_____; _____ (city) _____ (state)

2. Principals: The undersigned Buyer _____ agrees to buy and Seller agrees to sell, according to the indicated terms and conditions, the property described as follows:

3. Property: located at _____ (street address) (city) (state)

with the following legal description: _____,
including any of the following items if at present attached to the premises: plumbing, heating, and cooling equipment, including stoker and oil tanks, burners, water heaters, electric light fixtures, bathroom fixtures, roller shades, curtain rods and fixtures, draperies, venetian blinds, window and door screens, towel racks, linoleum and other attached floor coverings, including carpeting, attached television antennas, mail-boxes, all trees and shrubs, and any other fixtures, EXCEPT _____.

The following personal property shall also be included as part of the purchase: _____.
At the close of the transaction, the Seller, at his expense, shall provide the Buyer with a Bill Of Sale containing a detailed inventory of the personal property included.

4. Earnest Money Deposit: Agent (or Seller) acknowledges receipt from Buyer of _____ dollars

$_____ in the form of ( ) cash; ( ) personal check; ( ) cashier's check; ( ) promissory note at _____% interest per annum due _____ 19_____;

or other _____
as earnest money deposit to secure and apply on this purchase. Upon acceptance of this agreement in writing and delivery of same to Buyer, the earnest money deposit shall be assigned to and deposited in the listing Realtor's trust account or _____, to apply on the purchase price at the time of closing.

5. **Purchase Price:** The total purchase price of the property shall be _____ dollars $_____.

6. **Payment:** Purchase price is to be paid by Buyer as follows: Aforedescribed earnest money deposit ..... $_____

Additional payment due upon acceptance of this offer ..... $_____

Additional payment due at closing ..... $_____

Balance to be paid as follows: _____

_____

_____

_____

_____

_____

7. **Title:** Seller agrees to furnish good and marketable title free of all encumbrances and defects, except mortgage liens and encumbrances as set forth in this agreement, and to make conveyance by Warranty Deed or _____. Seller shall furnish in due course to the Buyer a title insurance policy insuring the Buyer of a good and marketable title in keeping with the terms and conditions of this agreement. Prior to the closing of this transaction, the Seller, upon request, will furnish to the Buyer a preliminary title report made by a title insurance company showing the condition of the title to said property. If the Seller cannot furnish marketable title within thirty days after receipt of the notice to the Buyer containing a written statement of the defects, the earnest money deposit herein receipted shall be refunded to the Buyer and this agreement shall be null and void. The following shall not be deemed encumbrances or defects: building and use restrictions general to the area; utility easements; other easements not inconsistent with Buyer's intended use; zoning or subdivision laws, covenants, conditions, restrictions, or reservations of record; tenancies of record. In the event of sale of other than real property relating to this transaction, Seller will provide evidence of title or right to sell or lease such personal property.

8. **Special Representations:** Seller warrants and represents to Buyer (1) that the subject property is connected to ( ) public sewer system, ( ) cesspool or septic tank, ( ) sewer system available but not connected, ( ) city water system, ( ) private watersystem, and that the following special improvements are included in the sale: ( ) sidewalk, ( ) curb and gutter, ( ) special street paving, ( ) special street lighting; (2) that the Seller knows of no material structural defects; (3) that all electrical wiring, heating, cooling, and plumbing systems are free of material defects and will be in good working order at the time the Buyer is entitled to possession; (4) that the Seller has no notice from any government agency of any violation or knowledge of probable violations of the law relating to the subject property; (5) that the Seller has no notice or knowledge of planned or commenced public improvements which may result in special assessments or otherwise directly and materially affect the property; and (6) that the Seller has no notice or knowledge of any liens to be assessed against the property, EXCEPT _____.

9. **Escrow Instructions:** This sale shall be closed on or before _____, 19_____, by _____ or such other closing agent as mutually agreed upon by Buyer and Seller. Buyer and Seller will, immediately on demand, deposit with closing agent all instruments and monies required to complete the purchase in accordance with the provisions of this agreement. Contract of Sale or Instrument of Conveyance to be made in the name of _____.

10. **Closing Costs and Pro-Ration:** Seller agrees to pay for title insurance policy, preliminary title report (if requested), termite inspection as set forth below, real estate commission, cost of preparing and recording any corrective instruments, and one-half of the escrow fees. Buyer agrees to pay for recording fees for mortgages and deeds of conveyance, all costs or expenses in securing new financing or assuming existing financing, and one-half of the escrow fees. Taxes for the current year, insurance acceptable to the Buyer, rents, interest, mortgage reserves, maintenance fees, and water and other utilities constituting liens, shall be pro-rated as of closing. Renters' security deposits shall accrue to Buyer at closing. Seller to provide Buyer with current rental or lease agreements prior to closing.

11. **Termite Inspection:** Seller agrees, at his expense, to provide written certification by a reputable licenced pest control firm that the property is free of termite infestation. In the event termites are found, the Seller shall have the property treated at his expense and provide acceptable certification that treatment has been rendered. If any structural repairs are required by reason of termite damage as established by acceptable certification, Seller agrees to make necessary repairs not to exceed $500. If repairs exceed $500, Buyer shall first have the right to accept the property "as is" with a credit of $500 to the Buyer at closing, or the Buyer may terminate this agreement with the earnest money deposit being promptly returned to the Buyer if the Seller does not agree to pay all costs of treatment and repair.

12. **Conditions of Sale:** The following conditions shall also apply, and shall, if conflicting with the printed portions of this agreement, prevail and control:

_____

_____

_____

_____

_____

_____

13. **Liability and Maintenance:** Seller shall maintain subject property, including landscaping, in good condition until the date of transferof title or possession by Buyer, whichever occurs first. All riskof loss and destruction of property, and all expenses of insurance, shall be borne by the Seller until the date of possession. If the improvements on the property are destroyed or materially damaged prior to closing, then the Buyer shall have the right to declare this agreement null and void, and the earnest money deposit and all other sums paid by Buyer toward the purchase price shall be returned to the Buyer forthwith.

14. **Possession:** The Buyer shall be entitled to possession of property upon closing or _____, 19_____.

15. **Default:** In the event the Buyer fails to complete the purchase as herein provided, the earnest money deposit shall be retained by the Seller as the total and entire liquidated damages. In the event the Seller fails to perform any condition of the sale as herein provided, then the Buyer, may, at hisoption, treat the contract as terminated, and all payments made by the Buyer hereunder shall be returned to the Buyer forthwith, provided the Buyer may, at his option, treat this agreement as being in full force and effect with the right to action for specific performance and damages. In the event that either Buyer, Seller, or Agent shall institute suit to enforce any rights hereunder, the prevailing party shall be entitled to court costs and a reasonable attorney's fee.

16. **Time Limit of Offer:** The Seller shall have until _____ (hour) _____ (date), 19_____ to accept this offer by delivering a signed copy hereof to the Buyer. If this offer is not so accepted, it shall lapse and the agent (or Seller) shall refund the earnest money deposit to the Buyer forthwith.

17. **General Agreements:** (1) Both parties to this purchase reserve their rights to assign and hereby otherwise agree to cooperate in effecting an Internal Revenue Code 1031 exchange or similartax-related arrangement prior to close of escrow, upon either party's written notice of intention to do so. (2) Upon approval of this offer by the Seller, this agreement shall become a contract between Buyer and Seller and shall inure to the benefit of the heirs, administrators, executors, successors, personal representatives, and assigns of said parties. (3) Time is of the essence and an essential part of this agreement. (4) This contract constitutes the sole and entire agreement between the parties hereto and no modification of this contract shall be binding unless attached hereto and signed by all parties to the contract. No representations, promises, or inducements not included in this contract shall be binding upon any party hereto.

18. **Buyer's Statement and Receipt:** "I/we hereby agree to purchase the above property in accordance with the terms and conditions above stated and acknowledge receipt of a completed copy of this agreement, which I/we have fully read and understand." Dated _____ 19_____. _____ (hour)

Address _____ _____ Buyer

_____ _____ Buyer

Phone No: Home (_____)_____ Business (_____)_____

19. **Seller's Statement and Response:** "I/we approve and accept the above offer, which I/we have fully read and understand, and agree to the above terms and conditions this day of _____, 19_____. _____ (hour)

_____ Seller

Address _____ _____ Seller

_____ Phone No: Home (_____)_____ Business (_____)_____

20. **Commission Agreement:** Seller agrees to pay a commission of_____% of the gross sales price to _____ for services in this transaction, and agrees that, in the event of forfeiture of the earnest moneydeposit by the Buyer, said deposit shall be divided between the Seller's broker and the Seller (one half to each party), the Broker's part not to exceed the amount of the commission.

21. **Buyer's Receipt for Signed Offer:** The Buyer hereby acknowledges receipt of a copy of the above agreement bearing the Seller's signature in acceptance of this offer.

Dated _____, 19_____ _____ Buyer

_____ Buyer

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The Nothing Down System of Creative Financing in Real Estate Investments

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SECTION N

Closing The Deal

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Closing the Deal



There are four major sources an investor can turn to for help and advice in closing his transaction:

A. REAL ESTATE OFFICES

Brokers are trained in preparing the paperwork necessary to complete any real estate transaction. However, in the United States the trend is quickly emerging that most real estate offices refer all of this kind of work to title companies and escrow companies. In Canada, the process of conveyance of documents, funds, etc., is usually handled by lawyers. If you are working through a real estate agent, he will make sure that all of the paperwork is handled correctly as part of the service he provides to make his commission. The tricky little details such as recording, trust deeds and trust deed notes, closing statements, etc., will be handled by a professional.

B. BANKS AND OTHER LENDING INSTITUTIONS

Whenever a refinance or a hard-money loan is involved, the bank or lending institution that is handling the loan may wish to handle the closing documents to insure that their interest is protected. More and more, however, the work is being delegated to title companies. The buyer and seller can choose a title company and give the name to the lending institution. In Canada, lawyers for the buyer and seller will communicate various transaction requirements to the financial institutions (i.e., banks, trust companies, credit unions, etc.).

C. LAWYERS

In some states (and in most Canadian provinces) it is customary for a lawyer to handle the closing. You will need to discover if this situation applies to your circumstance. Even if your area does not require the involvement of a lawyer, it is always a good idea to have a knowledgeable lawyer review the documents to make sure that everything has been handled correctly. A relatively small expense here may save you a $5,000 expense in the future.

D. TITLE COMPANIES (U.S. PURCHASES)

Where it is applicable to your area, a title company is your best source of closing information, as well as the cheapest. Title companies provide a variety of services.

1. Loan Information

Since the title officer has a chance to examine thousands of transactions in the course of a few months, he is extremely knowledgeable about real estate

financing, where money is available, which banks are lending on non-owner occupied property, and what interest rates are. It is always wise to establish a relationship with an aggressive title officer.

2. Title Policies

In most states it is the responsibility of the seller to provide proof of adequate and marketable title to his property. The normal method is to have a title company check the title at the county courthouse to verify that the seller can legally transfer his property to someone else. Then, this title is insured against any error, and the seller pays for this policy. The title company sells this insurance. Always request title insurance if it is available in your state. Once again, a small investment here can save thousands in the future.

3. Closing Services

Since the title company is involved in the title search, it is only natural for them to provide the other services surrounding the closing of the transaction. For a relatively small fee, they will handle the closing documents and the recording of these documents at the County Courthouse.

4. Trust Services

If your transaction requires the escrowing of documents for a long period of time (e.g., contract sales), the title company is the best source of trust (escrow) services.

5. General Information

One of the best sources of real estate information has always been my title officer. He is intimately aware of how the County Courthouse operates and can provide valuable information on how to use the information there to locate concentrations of don't wanters. He can also provide advice on how to use trust deeds and trust deed notes and other real estate documents. Much of this information can be obtained without charge to a regular customer. If you need help in creating paper against your own property or if you want to move a mortgage from one property to another, your title officer is the person to contact. You only need to understand the basics of the transaction. He will handle the details.

In my area the competition among title companies is fierce, and several officers offer a service called a listing package. It is primarily meant to be a service for real estate agents, but I find it invaluable for an investor. For no charge the title company will do some preliminary information gathering. They provide a copy of the deed, which is recorded on any piece of property I am interested in making an offer on. They can also find out what the yearly taxes are and who is the legal owner. Of course, they expect that if I buy the property, I will bring the transaction to their office for closing.

As a summary, the title company will be your best and cheapest source of information and service regarding the closing of your transactions. Nothing is too complicated or creative for them. They are fully aware of the ins and outs of double escrows, creation of paper techniques, substitution of collateral clauses, and any other creative technique that is taught in this course. All you need to understand are the basics of the transaction; the title company will handle the rest of the details.

E. CANADIAN PURCHASES

While title companies provide important professional help for real estate purchases in most areas of the United States, procedures differ somewhat in Canada. The matters of the search, setting up trust arrangements for documents and funds, recordings, etc., are handled by the respective lawyers of the buyer and seller, who rely on information received by title search through provincial Land Titles Offices. As in the United States, the title

search is critical to analysis of the title, in order to locate all liens, caveats, easements, and other forms of encumbrances.

Information about loans and money trends will be available from the real estate agent and from mortgage loan officers.

Creating Wealth

WITH LITTLE OR NOTHING DOWN

Manual

The Nothing Down System of Creative Financing
in Real Estate Investments

SECTION O

The Creative Generation Of Down Payment

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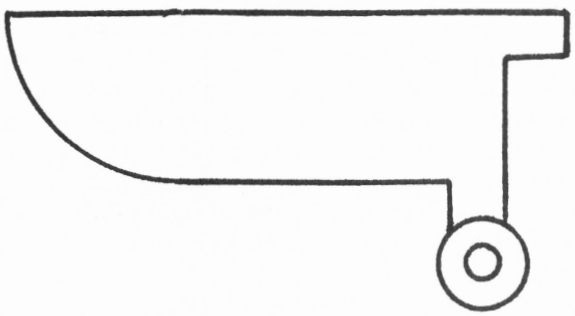
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Creative Generation of Down Payment

O

INTRODUCTORY NOTE

With this section we get to the heart of the "Nothing Down" System of financing. These are the creative techniques—fifty of them—for buying property with little or no money out of your own pocket.



Remember this sketch? It draws your attention to the need for a creative frame of mind. *Remember that creativity is the ability to solve problems in new and productive ways.*

By way of review, some of the key points about creativity are as follows:

1. Looking at situations in *novel* and *unconventional* ways.
2. Combining resources in *new* and *useful* ways.
3. A *positive* and *free spirit.*
4. Boundless *energy.*
5. *Exuberant, playful open-mindedness.*

Place yourself in a creative frame of mind as you review the "Nothing Down" techniques that follow. The techniques are organized according to the creative *source* of money for the transaction. We will review, in turn:

A. The Seller
B. The Buyer
C. The Real Estate Agent
D. Renters
E. The Property Itself
F. Hard-Money Lenders
G. Holders of Underlying Mortgages
H. Investors
I. Partners

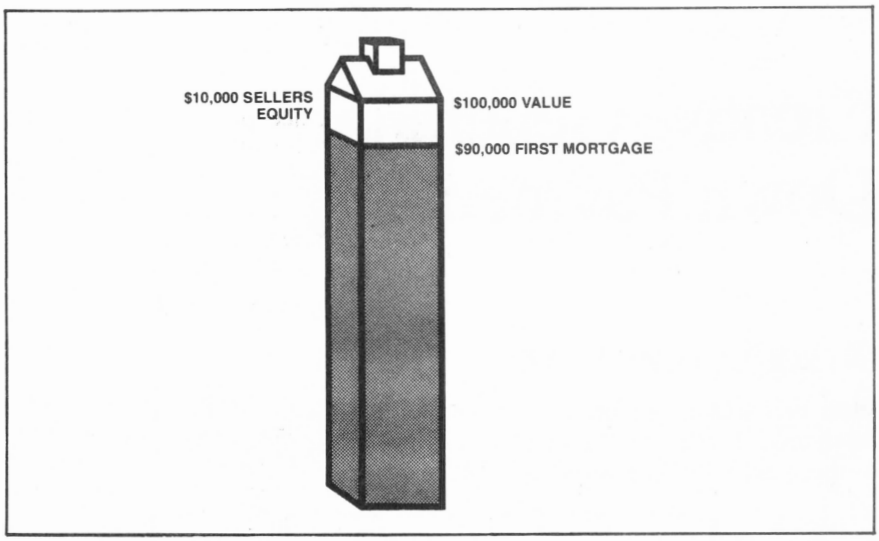
Take a deep breath! Here we go!

A. THE SELLER

1

◀ *Technique 1:*
The Ultimate Paper Out

The ultimate paper out: We're going to take an example of a $100,000 six-unit apartment building, where the seller has a $90,000 contract or wrap-around



mortgage that he is making payments on or is willing to create, and we have a $10,000 down payment that we must come up with. And our first offer to him is for him to take a $10,000 note for the entire equity with payments structured so that they can fit within our particular financial requirements. This doesn't happen every day. It's not something that we should expect in every instance, but it's something that we should ask for, because we never know what the seller is going to say. Perhaps he might go along with us.

2

Technique 2: ▶
The Blanket Mortgage

Technique number two is the blanket mortgage. Many times a seller will refuse to do a nothing down transaction with a buyer he does not know because he is worried about security. In his mind he can see you going into the unit and perhaps carelessly managing it, perhaps running it down, stripping it of its furniture and not taking care of it, letting the grass grow, and seriously decreasing the property's value. If you have nothing invested into this property, what is going to be the security for the seller that you will take care of it? You can generally alleviate the fears of a security-conscious seller by offering him more security than what he actually needs. In our example above we needed a $10,000 amount of equity to secure the seller with his down payment. Perhaps we could offer the seller a note for $10,000 to be paid on a monthly payment schedule with no down payment in cash. As for security for that note, we could offer the seller two pieces of real estate. Suppose we give him not only his own building but our own house with a $10,000 note secured against it. This is really called a blanket mortgage. There is a $10,000 face value note with $20,000 or $30,000 or $40,000 worth of equity to secure that note.

Now, of course, we don't want to encumber our house unless it's necessary, so we don't offer it unless we have to. But if the seller is security conscious, he may go along with it and say, "Okay, if you do default on this loan, then I not only get to repossess my building but I get to repossess your house." He can see that you are a sincere investor because you are willing to put your neck on the line. Of course, we don't want to tie up our property for a long period of time either. And so we should write into the terms of the note that if after one year of payments the seller has received all of the monthly payments on time and if the property has been kept in a satisfactory condition throughout this time, then the mortgage on your own piece of property will be removed. The property that the seller sold us will have increased in value, and there will then be more equity to secure this note, and the seller can feel comfortable. Perhaps, as an alternative, we can say to the seller that we will leave the blanket mortgage on both properties until the

purchased property increases in value to x number of dollars to be verified by appraisal.

3

◀ *Technique 3:*
Life Insurance Policy

Many times a security-conscious seller will not accept our nothing down transaction because he is afraid that if he does, we will be jeopardizing his security. Sometimes we can sweeten up that kind of seller by stating that we will purchase a life insurance policy with him as beneficiary, a policy that will completely pay off the amount of mortgage that we owe the seller in the event of our death. He is the beneficiary; we purchased the policy in his name; and therefore, he is secure. If anything happens to us, he will receive his money.

4

◀ *Technique 4:*
The Wrap-Around Mortgage

In our previous example, the seller was willing to create a wrap-around mortgage or a land sales contract or contract of sale (or agreement for sale, sales contract, etc.) of $90,000 that wraps around an existing first mortgage which he owes to his bank. Now although this is a very old and time-tested technique, it is still a very important concept for the creative thinker.

1. Capital Gains Advantage to the Seller

One of the greatest fears that a seller has is that when he sells his property, he will have to pay a significant amount of his profit to the government in taxes. Now capital gains taxes in the United States have been reduced to 40 percent (in Canada the current rate is 50 percent). Many unsophisticated owners have mistaken notions about this capital gains tax. In fact, it does not amount to 40 percent of their profits but means rather that 40 percent of their profitable gain will be added on to their adjusted gross income. Thus, the amount of tax the seller actually pays in the event of a sale is really not as much as he has imagined. (Even in Canada, where the capital gains tax provisions are not as favorable, the amount of tax the seller actually pays in the event of a sale may really not be as much as he has imagined.)

This approach can be a very powerful psychological tool. We can say to the seller, "Do you mean to tell me that you're going to sell and accept all the cash? Do you understand what will happen to your equity when you receive all cash from this sale? You will have to pay a significant amount of it to the government in taxes. There may be a better way for you to handle this investment. Perhaps you might consider selling it on a contract." And someone might say, "What is a contract?" "That is where I give you a small down payment, and you receive monthly payments instead of a lump sum cash payment. These monthly payments are taxed at much lower rates over a period of time. Your eventual tax burden can be extremely reduced." And this is true.

Another way of referring to this is the term installment sale or phased pay-out. By means of an installment sale, the seller may be able to spread his taxable gain over a number of years. There are, of course, rules to follow, and the matter should receive careful attention by a competent tax accountant. In general, however, the requirements in the U.S. are these: The payments must be made in two or more years, with any amount as the down payment during the year of sale. (Prior to the Installment Sale Revision Act, effective October 19, 1980, the total of "initial" payments made in the year of the sale could not exceed 30 percent of the selling price.) For tax purposes, the seller must claim in each year only the portion of any principal payment received that represents profit. A tax accountant can make sure all the details and rules are observed.

2. Further Incentives

We can offer the seller many incentives when he carries a contract. First of all, he will get some cash, and we can arrange for ways to pay this cash

without it having to come out of our pockets. Second of all, he receives monthly payments on the amount of his equity. Third, the $110,000 contract which he creates is in most instances at a higher interest rate than the amount of interest he has to pay on his underlying loan. He receives in this case an 11.25 percent interest on the entire $110,000 while he only has to pay 11 percent interest on his underlying mortgage, so he makes a spread of interest on an amount of money that he doesn't even own. This has a way of increasing his yield. In addition to that, his loan is going to be paid off much more quickly than our wrap-around loan. In fact, in our example, his underlying loan has 20 years left to pay on it, but the loan that he creates is for 25 years. Once his loan is paid off, then all the money that would have normally gone to pay off his bank now comes into his pocket, and he can enjoy it for the last five years remaining on his loan.

This is an excellent retirement planning tool. The benefit to the buyer by using this kind of a contract is that he doesn't usually have to pass through the types of extensive credit checks and the filling out of detailed bank forms. The closing costs on a contract are extremely inexpensive to the buyer and to the seller. And it's a much easier process to do; it can be done in a very short period of time. And so that's another benefit you can offer the seller—he can close on this property in three to four days, whereas if he wants me to go refinance, it may be as long as 60 days before he sees any of his money. These are the kinds of benefits that you can offer a seller to convince him to offer his property with little or no down payment.

5

Technique 5: ▶
Raise the Price, Lower the Terms

In this particular example, the seller has a property which he wants to sell for $100,000, and he wants $10,000 in cash. We may convince the seller that if he raises the price and lowers the terms, he might be in a better position. For example, "Instead of my giving you $10,000 in cash, Mr. Seller, which you may not need at this particular time, why don't I give you a $15,000 note? I will pay you $105,000 for your property. And you will receive a $15,000 note with monthly payments over a period of time and perhaps a balloon five to seven years down the road. You'll be making more money, more paper profit, your financial picture will be better, your financial statement will look more impressive, you won't be tempted to spend the money as you would if you had $10,000 in cash, and your tax picture will be even better."

Now this has to be done with a person who is sophisticated enough to realize that he actually makes more profit this way. This can only be done with a certain kind of investor who does not need cash, and you must realize that when you do this technique, you may actually be paying more for the property than it's actually worth. And you'll have to wait for a certain period of time in order to be able to start having any true equity built up in this property. It's probably wise to use this technique only when you know that the property is under-priced as is, and then you can go in and offer a higher price. This technique has a way of inducing the seller to go with your way of looking at things without involvement of cash.

6

Technique 6: ▶
The Balloon Down Payment

Our seller in this example needs $10,000 in cash. By giving a mix and match approach to all of the little techniques that we have been discussing thus far and will discuss in the next hour and a half or so, we can usually raise or whittle away the entire down payment. However, sometimes we find ourselves $2,000 or $3,000 short of the required down payment to buy. If we are not creative individuals, we will be tempted to say, "Obviously I don't have enough money, so I won't buy this piece of property." What you should understand is that many times it is possible for you to offer the seller the required short fall on your down payment, say $3,000, in the form of a short-term loan or balloon note. "Balloon" means having the note, without

payments, coming due at one particular time in the future. The entire amount is all due and payable at this one particular time. Any balloon note that is less than one year away from the original purchase will have the advantage of looking to the seller almost like cash. He can almost taste that money. He knows that it is coming soon. He can rearrange his schedule perhaps to move his requirements into the future for the payment with the money coming from that note. He can buy other pieces of property using that note, which is going to come due in the future as the down payment, and it is a way of giving you control of a piece of property with a short-term note so that you can do what you need to do with the property to either raise that $3,000 down payment or fix that property up and sell it before the note comes due.

1. Short Fuse Notes and Their Risks

Short-term balloons might be referred to as short fuse notes. Anything less than about two years is a short fuse note. As one person said, "If you would like to make winter go quickly, arrange to pay a $50,000 balloon note in March." The winter will speed by faster than you can imagine. The reason we call them short fuse notes is because if they are not handled carefully, they can blow up in your face. It is not wise to have short fuse balloon notes unless you know where the funds are coming from. It is a little more of a gutsy technique and should be used very carefully and very wisely. However, if you find yourself in a situation where you can't buy a piece of property without using a balloon note and you feel you have enough leeway to protect yourself, by all means use the balloon note and buy the property. In times of higher inflation, it's better for you to buy the property and take the risk than for you not to buy the property and let inflation eat you alive. See Section K, Item D for more details.

7

◀ *Technique 7:* High Monthly Down Payments

Many of you who do not own real estate might have an income that allows you leeway to save several hundred dollars a month from your monthly salary toward the purchase of an individual piece of property. And many of you may have been tempted in the past under the conservative approach to save this $150 or $200 a month and put it into a special savings account, hopefully for the eventual purchase of a small piece of real estate. By saving $200 a month you can generate with your interest earnings approximately a $5,000 down payment in a two-year period of time. And that $5,000 down payment could probably purchase for you some small piece of real estate.

Now, what happens two years from now? Who knows what piece of property you'll be able to buy with a $5,000 down payment? Maybe none at all. And in that two-year period of time properties might have increased perhaps $10,000 to $15,000. Why don't you take advantage of your monthly cash flow now by making high monthly down payments on your piece of investment property. Go to the seller and say to the seller, "I can pay you $200, $250 on a note, and I can pay it off quickly. But I would much rather buy a property from you now and give you my high monthly down payments than for me to go save that money for a two-year period of time." Some sellers may be receptive to this kind of plan. Maybe they are short a couple of hundred dollars a month in their particular needs, and this two- or three-year savings plan for them would be just what they are looking for. This is a forced savings plan. It forces you to get your money invested into real estate, and it forces you to sacrifice your money for an investment that is going up in value. It takes away the temptation of spending your savings on things that go down in value. So that's high monthly down payments.

8

◀ *Technique 8:* Defer the Down Payment with No Mortgage Payments

This is a very interesting technique and comes out of our interviews with our past graduates. One of our graduates wanted to buy a piece of property, a six-unit apartment building, but the seller who owned the property free and clear was not willing to sell with no down payment. He felt that it was

important to get at least a $10,000 cash down payment on the front end to make his investment secure. He did not need the money; he did not even need the cash flow from his free-and-clear apartment building; he just had decided it was time for him to retire and to get rid of the property.

Our student analyzed the situation and noticed there might be some flexibilities in the requirements of the seller. First of all, he did not need cash now, but he wanted a $10,000 down payment, but only for his security. Secondly, the property was free-and-clear. He then approached the seller with this kind of offer: "Mr. Seller, I would like you to sell me your building now with a $10,000 down payment to be paid to you in seven months and with the first mortgage payment coming due eight months from now with the interest that is accruing on the amount of money I'm borrowing from you to be accruing on the total long-term mortgage." The seller agreed to that type of offer and let this student assume the management of this property. Well, without a mortgage payment to make, the student was able to pocket all of the rents and all of the deposits, and since he did his own management and took care of his own maintenance expenses, he was able to put most of every dollar he collected in rents into a savings account. At the end of his seven months' period of time, he had saved approximately nine-tenths of the required down payment. He had to come up with only a very small amount of money out of his pocket, and then the first mortgage payment was due one month thereafter. The seller got his $10,000 in cash, plus monthly payments coming in from the building. He just gave the buyer the opportunity to let the building generate the down payment for him. This again is another way that the seller can be flexible in the way the property is purchased. This ends the section on seller flexibilities; let's go to the next section, which is buyer flexibilities.

9

B. THE BUYER

Technique 9: ▶ Your Own Savings and Inheritances

The first technique under the resources of the buyer is the use of personal savings or inheritances. Obviously, this is not a very creative generation of down payment, because it requires sacrifice, and the entire purpose of our course is to be able to avoid the use of our own cash if at all possible. However, we find from time to time that we have to use some of our own cash. And we should be in the habit of saving at least 10 percent of the amount of money we earn to use toward investment purposes. It is wise to have some savings which are kept as a cushion against eventual problems, and this cushion should never be touched, except in extreme emergencies. This gives each and every family a feeling of security in knowing that they have a little nest egg that they can fall back on. Several of our students have gotten themselves into financial difficulty because they borrowed indiscriminately. However, one creative variation on generating funds from your own deposits is to borrow using them as collateral. The process of collateralizing a loan with cash deposits has the advantage of leaving your funds intact (or with money market funds that foregoes penalties for early withdrawal).

10

Technique 10: ▶ Supply the Seller What He Needs

In our initial discussion with the seller, we ask questions such as, "What are you planning to do with the funds you receive as down payment?" "Are you planning to buy any furniture or any other items that may be purchased for less than $1,000?" "Are you planning to buy any cars or any other such items?" "Do you plan to purchase household goods for your brand new home?"

The reason that we ask these questions is to determine whether or not we might be able to use our existing credit to borrow against in order to purchase the seller the kinds of things he wants. If he is going to take our money and go purchase the items, why not let us go down with him to a local

department store or the local car dealer to buy him his needed items. We use our credit, not our cash. We could even buy a car for him to drive with us handling the monthly payments. We could put purchases of up to $1,000 on our MasterCard and VISA card and repay the amount over a period of months.

11

◀ *Technique 11:* Assume the Seller's Obligations

Many times a seller is selling so that he can get himself out from underneath the burden of inordinate debt. Sometimes many conservative property holders cannot stand the feeling that is caused when there are so many obligations. Although these obligations may be paid back on a monthly basis, they don't like the feeling of owing people money. We could step in since we are in the business of borrowing money and assume these obligations that belong to the seller. This eliminates our need for cash. He may have a $1,000 line of credit with his bank that he is making payments on at $77 or $80 a month. He may have a Sears account which is overdrawn or used to its limit. He may have debts to private individuals. He may have debts to previous purchasers. Maybe he just wants to get himself into a more liquid position. We can help him out by placing these obligations on our financial statement and removing them from his.

In one situation on a purchase that I made several years ago, a seller had $11,000 worth of bank loans that he was repaying on a monthly basis, and he wanted to have those paid off entirely in cash. I simply asked him, "Can I assume these loans?" He saw my solution, and I assumed the payment on these loans and saved myself the problem of having to come up with $11,000 which I didn't have.

12

◀ *Technique 12:* Using Talents, Not Money

Many of our students are real estate agents. They know full well that any property in the real estate listing book can be bought by any agent and that they can apply a portion of their commission toward the required down payment. There are other types of situations where a professional might be able to use his or her professional services as portions of the down payment. Dentists can give prepaid credits toward the use of their services in the future for a family plan. A doctor might be able to deliver a baby or two or give professional advice or counsel. You might have a particular skill that no one else has that might be of great benefit or use to the seller.

This is why you ask the seller what he is going to do with his money. You ask him questions with respect to your particular skills to see if he might have need of them. You might be a lawyer and be able to reduce your fees for services in the future. You might be an accountant and be able to apply your fees toward the future auditing of business records. At least a portion of every real estate down payment may be applied toward the use of services in this manner. You also might have certain particular skills such as a carpenter or a brick layer or a mason, or you could clean up or do almost anything with your two hands.

1. A Case History

One of our graduates by the name of Sam Hall located a small one-bedroom home that he wanted to buy from the seller. The seller set a price of $28,000, and the bank told him that they would not lend on a one-bedroom house—although before they turned it down, they did appraise the house for $20,000. He thereafter went and made arrangements with the seller that he would pay $18,000 in cash as a down payment for this small home if the seller would carry back a $10,000 personal note to be paid off at some time in the future. Then he obtained permission from the seller to come in with his own tools and with his own time and add another bedroom onto that one-bedroom single family house.

After he added a second bedroom and cleaned up the property con-

siderably, he went back to the bank and made application for a new loan. The appraiser came out and saw that there were two bedrooms and reappraised that exact same home only months later for $44,000. Sam was able to use his skills to enhance the value of the property. He now borrowed $28,000 against that $44,000 home and gave $18,000 to the seller in cash and put $10,000 of the proceeds of the loan into his own pocket. He succeeded because he used his talent, not his cash. In addition, when he applied for the $28,000 mortgage, he had the bank mortgage only the front half of the extra large lot, leaving a free-and-clear $12,000 building lot to use as additional capital. He was able to use a lot of creative thinking to generate a creative profit.

2. Ideas for Retailers

Many of you belong to businesses where you can purchase goods at wholesale prices, then turn around and sell them or trade them at retail prices, e.g., a food storage business, or a grocery business, or a clothing business, where you can buy goods at 50 percent of retail and trade them at full face value. If you own a clothing business, you might be able to tell the seller that he could come in and select up to $5,000 worth of clothing over the next period of years, at any time he wished, for a credit of $5,000 toward the down payment on his property now. Use your ingenuity.

13

Technique 13: ▶ Borrow Against Life Insurance Policy (Yours or a Partner's)

Do you have life insurance policies with cash values tied up in them? It is very unwise to leave this money tied up where it earns about 3 percent interest. Borrow it out and use the money to buy real estate. You may think that this is unwise and a non-conservative approach to your insurance needs, but it is not. In the event of your death, your spouse will be able to sell the real estate that you have bought by borrowing against your life insurance policy and should definitely be able to come out ahead, if not even do much better than your life insurance policy. Assume that your borrowings are another way of assuring the security of your spouse in the event of your death.

If you do not have a life insurance policy to borrow against, it is possible that a relative or friend has one with cash value in it that could be accessed. If so, you could arrange to borrow an amount equal to part or all of the down payment in exchange for an appropriate interest incentive for the policy owner. By teaching a person how to make more profitable use of his or her cash value funds, you help him or her win while solving your own down payment problems.

14

Technique 14: ▶ Anything Goes

Those of you who have filled out your financial statement should have included all the dead equity items that you have but do not seem to be using. I have known many of our graduates who have recreational properties that they never use. Some have cars, boats, stereos, and other personal property. One lady in Phoenix, Arizona, had a brand new Cadillac that she didn't use very much. She didn't like its gas mileage, so it was a burden to her. Can you see how she could casually mention to a don't wanter that he could have the keys and the title to the beautiful car in his driveway if he would just sell his property with the car as a down payment.

I have heard of cars, trailers, and motorcycles being used as down payments. What do you have?

15

Technique 15: ▶ The Creation of Paper

This technique involves the use of the equities that you own in real estate. How can you use your equities to the fullest advantage? If you were to go down to your local finance company and borrow out your equity, you would find that it is very difficult to borrow your entire equity. You have to pay high interest rates; you have to fill out long and tedious forms with credit checks; you have to pay back this money in monthly payments over a very short

period of time, and it is generally a very unpleasant experience. However, using the creation of paper technique, it is possible to be able to borrow 100 percent of your equity in any property that you own with very low interest rate loans over long periods of time with very minimal credit checks and paper work.

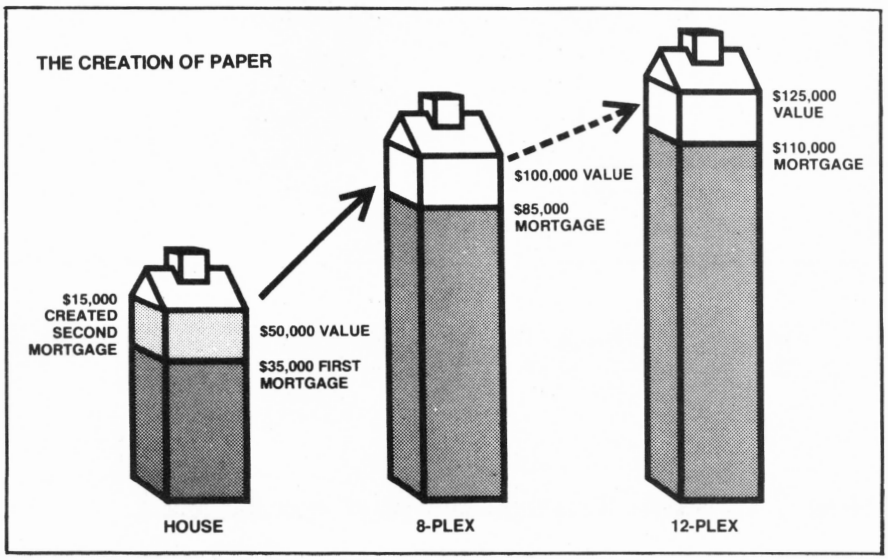
1. Trust Deed Notes (or Mortgage Notes)

The creation of paper technique involves the use of trust deed notes and trust deeds (mortgages in some areas). If you have a home that is worth $50,000 with a $35,000 first mortgage, you have $15,000 worth of equity in it. If you can locate someone who is a don't wanter and wants to get out of his property, you can offer him a $15,000 note secured by the equity in your own home as a partial down payment for the equity in his property. What you are doing is creating value out of thin air by sitting down at your typewriter and creating a note for $15,000 with payments to be negotiated and a trust deed (mortgage) for security. The note is signed, and the trust deed (mortgage) is notarized and recorded at the courthouse (in Canada, at the Land Titles Office). It's simple, easy, and costs you only a recording fee at the courthouse, plus the cost of the documents that you can buy at any stationery store.

Sellers rarely ask for any type of credit check on a creation of a note in this manner, although they may wish to obtain a title search on your property to see if you are the legal owner. It's very possible to use your equity as down payments on any investments as long as the seller is willing to accept this as partial or complete down payment. This allows you to borrow against unborrowable assets or borrow against unborrowable credit ratings. It gives you the flexibility to fix up the property that you are buying with these notes, to sell the property for cash, thereby raising enough dollars to use in your buying program. It provides pyramiding potential. It allows you to borrow dollars out of your property without having to sell your property.

By borrowing the entire equity in my home, I am encumbering my equity and therefore am not able to use that equity for any other purpose. This may seem a little unusual to some of you more conservative investors, but as you will learn later, it makes no sense to have any equity in a piece of property unless it is entirely free and clear. If there is any loan on it, then the only kind of loan that makes any kind of sense is to have a 100 percent loan. We need to use all of our resources as much as possible to help pyramid us into a net worth that we can retire upon. Then we can worry about making our properties free and clear but not until.

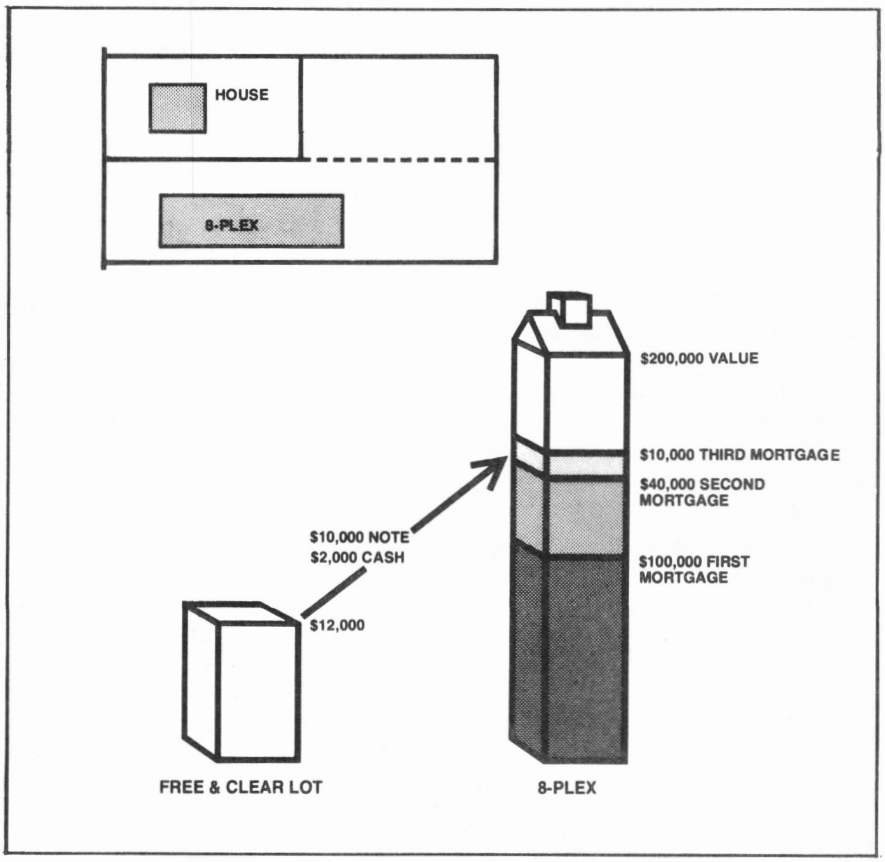
The creation of a note is a very simple and straightforward act. If you are not comfortable with drawing it up yourself, you can go down to any title company or lawyer of your choice and have it done for you.



2. A Case History

Let's see how the creation of paper actually works using a student example. A student was approached by a neighbor. His neighbor owned a home with a very deep back lot which had gone to weeds. He did not wish to cultivate it, so he approached the student and asked him if he wouldn't want to buy the back end of his lot and get permission from the city to build a four-unit apartment building there. Next to this lot was my student's eight-unit apartment building as you can see from the illustration below.

The neighbor asked the price of $12,000 for this free-and-clear lot. The student, being a creative individual, realized that there might be a no-cash solution here. He offered the seller a down payment of $2,000 in cash in three months plus a "created" third trust deed (mortgage) on his own eight-unit building. The neighbor, who realized that he had no other choice, accepted and delivered the lot free and clear. The student now went to a lending institution and made application for a building or construction loan to be able to build a new four-plex. Out of the construction loan he withdrew $2,000 to pay the seller off. He then was able to build his four-plex with just barely enough money to complete the building without having to come up with any, or only very small amounts, of money out of his pocket.



If you have equities like this, you can use them. You can borrow against them. You can use them in creative ways.

Note: See Section R for techniques 16-18 on exchanging.

C. THE REAL ESTATE AGENT: A TECHNIQUE FOR BORROWING THE COMMISSION

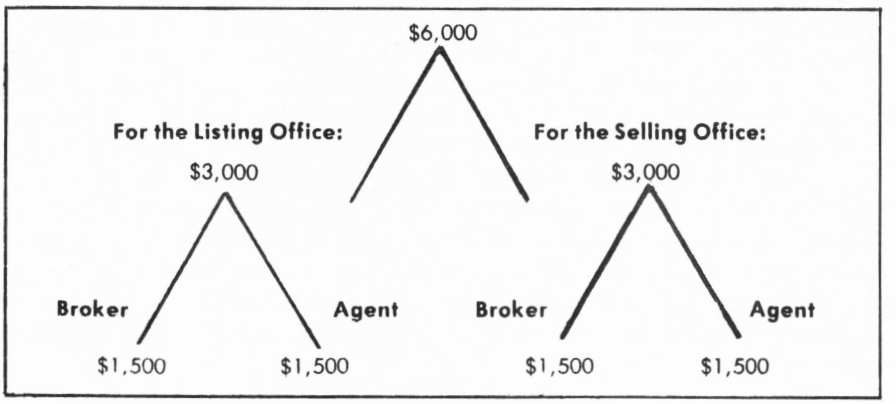
19

◀ *Technique 19:*

In most instances, the largest cash outlay expense that a seller has is the real estate agent's commission. As was described earlier, the real estate agent, in some instances, may be amenable to letting you borrow a portion of his commission to be applied toward your down payment. Let's take an example of a $100,000 building. If I had a 6 percent commission that needs to be paid to the agent, then that means that the seller needs $6,000 to pay to his agent. Where does the seller get this cash? From the buyer. If the seller is selling for a 10 percent down payment or less, most of the down payment will be commission. If we understand that the agents involved may lend us their commissions, we have just raised a major portion of the down payment necessary to buy the property. I don't misuse this knowledge, but I refer to it when it is necessary.

1. Dealing with the Listing Agent

I try to deal as much as possible with the listing agent if I'm going to be able to use this technique to its fullest advantage. The listing agent stands to make the largest commission if he sells the property himself. Under the MLS rules in almost every U.S. or Canadian city, approximately one-half of the commission paid will go to the listing office. The other half of the commission will be paid to the selling office—in this case $3,000 to the listing office, $3,000 to the selling office.



However, if the listing agent lists and sells the property, he stands to make a sizeable commission. By listing it in the MLS book, he has already psychologically agreed to split that commission, or $3,000 of it, with the selling office. We therefore know that he expects to receive approximately $3,000 in cash. If we can convince him he will receive the $3,000 in cash and a note for $3,000, then we have just saved ourselves from having to come up with $3,000. I know of circumstances where 100 percent of the commission has been borrowed from the real estate broker involved so that the transaction could go together. The payment of commissions in the form of notes can't be all that bad for agents since a monthly payment can go a long way toward helping an agent fill in his income with a steady cash flow. And if he doesn't agree to my suggestion, then perhaps I can't buy the property. That can be your leverage with him.

2. What to Do if the Real Estate Agent Balks

If the real estate agent balks at lending you some of the commission, you might offer to increase his commission—$3,000 now and $3,500 in the form of a note payable in monthly payments over the period of a few years. One of our graduates was having trouble getting a transaction together and needed

an extra $3,000 or $4,000 in cash. The agent offered to lend the cash to the student and went to a relative and borrowed the money to get the deal to go together. It's amazing how the real estate agent can enter in and try to solve the problems.

20

Technique 20: ▶
Rents: The Automatic Down Payment

D. RENTERS

Did you know that there is an automatic down payment built into every real estate purchase? The renters of the building you are buying will help you buy the property. This circumstance arises out of a very unusual quirk in the way property is purchased. Mortgage payments are not due for at least 30 days after the initial purchase of an investment piece of property. This is so because there must be time for interest to accrue on the loan. This is not true, however, of rents. Rents are due the day the renter moves in and are amortized over the next 30 days. Rents are paid in advance; mortgage payments are paid in arrears.

In our example where we have a six-unit apartment building and the rents are $250 a month, I have a situation where I'm able to collect as much as $1,500 rent the very day that I buy the property. I can take this rent and use it as a portion of the down payment. On one purchase I was able to collect about $10,000 using this method.

21

Technique 21: ▶
Deposits

In addition to that, I might have security deposits that I'm able to collect and also put in a bank account. This may be as much as $150 per unit or more. And six times $150 is $900. The second I buy that particular six-unit apartment building I may have as much as $2,400 in a separate bank account which belongs to me ($1,500 for rents and $900 for deposits). That amount of money could be creatively used as a down payment to buy the property in the first place. The seller sells the property with a $10,000 down payment and hands me over an apartment building and a bank account with $2,400 in it. I just turn around and give him his $2,400 back, and therefore, I reduce my down payment by $2,400. As soon as the next month's payment is due, I collect the rent as usual and subtract out enough money to pay my first mortgage payment and pay enough money for my expenses, and I continue as usual.

1. Dealing with Moving Tenants

If a tenant moves, I have already spent his security deposit in the initial purchase price. So where do I get the new deposit to pay him back? I have an agreement in my leases that states that the deposit will not be sent back for at least 15 days. The reason for that is two-fold: (1) I want to be able to make sure that there are no bills that come back to me that were not evident when the renter moved out of the property. I also want to make sure that he has cleaned the property carefully so that I don't have to pay for it out of my own pocket. (2) I want to be able to have time to rent the property to a new tenant and thereby collect his rental deposit and turn around and send his new deposit to the old tenant. I therefore keep that same amount of security deposit rolling *ad infinitum* as long as there are tenants moving in.

2. The Legal Implications

Now in some states or provinces it may not be legal to co-mingle the tenant security deposits with the rental account, and therefore, the use of rental security deposits as down payments is not possible. But in other areas such as California, Washington, Utah, and many others, this is possible and is an excellent source of down payment. You should familiarize yourself with prevailing legislation for your investment area.

E. THE PROPERTY ITSELF

The next area of discussion is the property itself. The property has in some limited circumstances the ability to provide a down payment for the buyer if he knows what he's looking for. I suppose the best way to describe how this works is to go through an example.

22

◀ *Technique 22:*
Splitting Off Furniture and Other Items

One of my close friends recently purchased a 30-unit apartment building and found that it was filled with some very, very choice antique furniture that had been painted over. He negotiated with the seller to let him come in and assume the management of the property and pay him a $20,000 down payment six or eight months down the road. Then this friend went in and had all the antique furniture removed and stripped and refinished and then placed in an antique furniture store and thereafter sold. The net profit from that particular venture was approximately $20,000, which was enough money to provide a substantial down payment on the piece of property and was the way for him to buy that property without having to involve any of his own cash. Of course, you ask yourself as you are looking through the property, "What does this property have that may be sold off? What has value among its personal property items?"

One of my recent graduates approached me after the seminar and said that he had been thinking a lot about this one technique and knew that there was a house for sale down the street from him out in the country where the seller seemed to exhibit the signs of don't wanter-itis. The student wanted to know if it might be possible for him to use these techniques to buy this property with nothing down. I told him to ask questions and probe, and he indicated that there were two very large black walnut trees growing in the front of that house that he felt could probably be cut down and sold as fine furniture wood for about $1,500 a tree. Well, automatically there's $3,000 that could be generated somehow to help finance the down payment on that property. You may have to sacrifice the trees to do it, but if you don't have any money, that might be the only source you can look for.

One of the real estate agents at a recent seminar told me that he once sold a small motel to a client who did not have any cash. They went to a bank and borrowed the necessary cash for a down payment by putting up the motel furniture as collateral. The real estate agent took a note for the commission, and the buyer bought the building with nothing down.

23

◀ *Technique 23:*
Splitting Off Part of the Property

One of my more creative transactions involved the buying of a piece of property that had a large back lot. The seller indicated to me that she wanted a very large down payment in cash, and by using a combination of the techniques I was able to reduce my cash outlay for getting into the property to about $2,000. Then I asked her about her property. I asked her, "Is there anything that is unusual about this property that may generate some cash using a splitting technique?" And she said that she had been recently contacted by a next-door neighbor who wanted to purchase the back end of her lot and use it as a garden; and since it was just a rental home, he didn't feel that there would be anything wrong in selling the back end of her lot. She had done some preliminary negotiation with him and even had gone so far as to get a survey to split off the back 30 or 40 feet and to get permission from the city to have the split done. And then, of course, she decided to sell the property because she was a don't wanter and wanted to get rid of it quickly and therefore did not pursue the sale of the lot.

I decided to pursue it to see if the fellow was really interested in buying the back end of the lot and found out that he was interested. He called me and indicated that he would be willing to pay $1,500 for the back end of the lot. I told him that I needed $2,900 in cash, or I would not even be interested,

so he went to his credit union and borrowed $2,900 cash to be delivered to the closing agency (in this case a title company) as of the date of the closing.

1. How to "Sell" Something Before You Buy It

Now there are some technical aspects that are necessary to understand here. First of all, I cannot sell a piece of property that I do not own. So the first thing that is necessary is for me to be able to own that entire piece of property. Then I have the legal right to split off a portion of it to him for his payment of $2,900. So he delivered the $2,900 to the closing agency (title company), and with that money I was able to buy the property and put it in my name. I took $2,000 of the money he gave me, and I gave it to the seller, and I kept $900 for myself as proceeds from the sale of the back of the lot. I had sold off a back portion of that lot before I had even purchased it, and I used the proceeds from this sale to buy the entire property in the first place.

2. Getting a Release of Mortgage Against the Split

The second problem arose when we found that the mortgage company that held the mortgage on the entire piece of property was not willing to release their mortgage on that back end. What it required then was a brand new appraisal on the front piece of property to make sure it wasn't being reduced in value by the split. This required a new survey and permission from the city. With these documents submitted to the loan company and payment of a release fee (in this case $100), we were able to get the back end of the lot released, and I was able to transfer to this neighbor a free-and-clear piece of property that he could now use for his garden in return for the payment of his $2,900 in cash.

3. Inducements for the Buyer of the Split

The only remaining problem was that he was not able to receive clear title to that property for several months after my purchase because it took several months worth of paper work to get it through. So in order to secure his $2,900 investment in this land, I gave him a created second trust deed note (mortgage) against one of my buildings, bearing zero percent interest. Thus, if I had any trouble splitting the back lot off, I could just pay him his $2,900 back and thereby complete the transaction.

4. Be on the Lookout for Variations of the Split

If you ever examine a piece of property that seems to have additional land attached to it which may be used for other purposes, such as an additional building lot, etc., but it is tied up under an existing mortgage, you may consider refinancing your property and having the new mortgage only cover the amount of property that you want to encumber, thereby leaving the additional piece of property free-and-clear to dispose of in any manner you see fit. You could feasibly have the property sold with its closing time coinciding with the purchase date of the property you're buying. This is just another splitting technique. It's a way you can raise down payments for the purchase of a piece of property before you even buy it. I'm thinking now of a graduate of mine who located three duplexes that were $10,000 each under the market price. His initial creative idea was to tie up the three duplexes with a three-month closing, to turn around and re-sell two of the duplexes and make a $10,000 profit on each, and use the $20,000 in profit as a down payment to purchase the third duplex. This is just another splitting technique.

5. A Half-Million-Dollar Case History: The Partial Release

Another one of my students described in class how he had located a whole block of investment houses which was owned by Safeway. Safeway had gone in and had tried to rezone this entire block for conversion into a Safeway grocery store. Therefore, they had gone in and purchased all of the 10 or 15 or 20 houses around this block with the idea in mind of demolishing them and turning the land into commercial land. They purchased all the houses and then had been turned down by the city for rezoning. So they put the property

back on the market for the price of about $600,000, expecting to be cashed out. They owned it free-and-clear.

My student went in and negotiated with Safeway to let him give them $100,00 down payment and carry the remaining $500,000 at 6 percent interest for a period of years, which would give him plenty of time to go in and resell all the properties and fix them up. How did he raise the $100,000 down payment? He used another old technique called the partial release. He convinced Safeway that if he were to give them $100,000 in cash, they would have to release three of the houses from the underlying mortgage of $500,000. In other words, if he gave them $100,000 in cash, they would have to give him three free-and-clear houses. He therefore went and *prearranged* the sale of each of those three houses to *prearranged* buyers and collected $100,000 in cash at about $30,000 or $35,000 a house. He then gave Safeway $100,000 as a down payment, thereby releasing the three houses to the new buyers, and he obtained the entire rest of the block with no down payment and with a note at 6 percent interest! He could then go in and fix up the houses as he wished, rent them out as he wished, and it was my understanding that he went in one by one, fixed each one up, then turned around and sold it and created a job for himself as he sold these houses off. That's called the partial release.

Splitting is a very widely understood technique in the development business but very little understood in the layman area of real estate. And it only takes a little bit of creative imagination to know how to recognize creative nothing down possibilities.

F. HARD-MONEY LENDERS

Now we'll go into the next section, which deals with lenders: how to use short- and long-term lenders to help you get into properties with none or very little of your own money involved. Nothing down does not mean that the seller does not get cash. We have given you over 20 techniques up to this point which involve the use of extremely small amounts of cash or no cash whatsoever. However, there will come a time sooner or later when you're going to have to come up with cash for that investor or that seller who needs it. And you are going to have to go to your short-term lenders to obtain hard-money dollars.

1. Obtaining Short-term Loans from Hard-money Lenders

◀ *Technique 24:*
Small Amounts of Money from Different Banks

24

The first thing we will describe to you is the technique of borrowing small amounts of money from several different banks.

a. Credit Doesn't Happen; It Has to Be Built! The following chart outlines the process for establishing up to $25,000 of unsecured credit (immediate signature loans) at a combination of banks.

Short-Term Funds from Hard-Money Lenders

How to build your credit:

A. Choose five banks in your area immediately.
B. Pick a loan officer you can relate to.
C. Go to another bank if you feel you are not welcome.
D. Ask your loan officer if he owns real estate.
E. Determine what the loan officer's credit limit is.

F. Ask him if it is possible to establish an unsecured line of credit. If so, how long does it take?

G. Borrow as much as you can either secured or unsecured as soon as possible.

H. Repay your loans early but not too early.

I. Repeat the loaning process with a larger amount.

J. Goal: *to be able to borrow $5,000 from at least five separate banks simultaneously within two years.*

As you build up credit and establish a reputation as a dependable borrower, it may be possible to cultivate the kind of relationship with this or that banker that will enable you to finance your real estate investment program through a *single* bank. Until you have progressed to that point, try the multiple-bank approach in order to grow as rapidly as possible and test relationships for the best "fit."

b. Some Tips on Establishing Credit.

(1) Banks are keenly competitive so don't be afraid to shop around for a cooperative banker.

(2) Cultivate close relationships with your loan officers: learn to appreciate their frame of reference. Send them referrals and take credit for it.

(3) Don't be duped by the ads—those friendly bankers are cooly security conscious. "The people who are writing the ads aren't making the loans." When you find a cooperative banker, treat him like gold.

(4) Come prepared with all of the details: financial statements, income tax statements, pictures of your properties, etc.

(5) Don't fudge—be realistic about your assets. Build up trust and credibility.

(6) Keep it simple. Spare him the details about your creative financing plans. "A confused mind always says 'No.'"

(7) Keep him abreast of your progress—let him know you're a good risk.

(8) Begin with a $500 deposit at one bank, then use this as security for a $500 loan, which you could deposit at another bank in order to continue the process. You could involve four or five banks in this way. Then increase the size of the loan for the next round. Build up a credit line of $5,000 and more at several banks in a short time. Of course, some banks may have a policy of loaning for "designated" purposes and making the payment directly to the creditor. Shop around for the most flexible policy.

(9) It is best to contact a bank officer who has at least a $5,000 lending authority. (Don't open the accounts with the person assigned to do this—make an appointment to see the officers with more authority.)

(10) Let the bankers know of your plans—ask their advice on building up credit, good investment opportunities, etc.

(11) Build up credit when you don't need it so that you can borrow quickly when you do!

(12) Gradually increase the amounts of the notes until you can quickly borrow unsecured funds to take advantage of the good bargains that come your way.

"A man's worth is measured
not by how much he has,
but by how much he can borrow."
—Robert Wells

◀ *Technique 25:*
Cash-By-Mail Companies

25 - 29

These institutions sometimes advertise in airline and executive magazines. The loans are unsecured, but the rates and monthly payments are high. To qualify, you must have a substantial income and must not be self-employed. Two examples of such an advertisement are reproduced below.

People who earn $20,000 shouldn't have to go to a bank for a loan.

Now you can apply for your own loan by simply filling out this coupon or calling the toll-free number below.

After all, if your income is $20,000 or more per annum, why should you waste time explaining your finances in person? At FinanceAmerica we make quick, confidential loans up to $15,000.

You might even say we've invested a lot of time making it easier to get a loan.

FinanceAmerica
We invest in you.

Name_____

Address_____

City_____ State_____ Zip_____

Mail coupon to: 3717 South Western Avenue, P.O. Box 95066, Oklahoma City, Oklahoma 73143

800-654-3975
Continental U.S. only
In Oklahoma call 405-631-4401 collect. TW-10

FinanceAmerica VIP Service Corporation

A BankAmerica Financial Service Company

Immediate Action
... one of the reasons executives and professionals select Beneficial for
LOANS UP TO $15,000

Other good reasons:
- Strictest privacy. • By mail or phone.
- Complete discretion. • Personal, unmarked mail. • Competitive rates.
- Flexible, convenient payment schedules.
- No pre-payment penalties.
- Capitalized by Beneficial Corporation.

Beneficial Executive Loans $2,000 to $15,000, especially for incomes $25,000 and up. In California phone collect **408-247-8666.** Outside California phone toll-free 800-538-6811 or write: Don Nemiro, Director, 2858 Stevens Creek Blvd., Suite 1, San Jose, CA 95128, Dept. WJ-244.

Beneficial Executive Loan Services
Division of Beneficial Finance Co. of Northern California

◀ *Technique 26:*
Credit Cards

It is possible to qualify for more than one of the various cards at a time (MasterCard, VISA) through separate banks. Several thousand dollars of credit could be available in case you might want to provide a seller with needed items, assume his obligations, etc., as part of the down payment.

◀ *Technique 27:*
Home Improvement Loans

Lending institutions regularly make secured loans for the purpose of home improvement. Unless there are stipulations to the contrary, parts of these funds could be used to good advantage in investment activities ("fix up" needs, etc.).

◀ *Technique 28:*
Home Equity Loans

One of the best sources of capital for the beginning investor is the equity in his home. Lending institutions regularly make second mortgage loans secured against home equity for worthwhile purposes. Normally as much as 80 percent of the equity can be borrowed.

As an example, consider a family that owns a home valued at $80,000 with a mortgage of $30,000 on it. They check with a number of lenders and locate the one with the lowest interest rate and longest repayment period, say, $10,000 for 10 years at 16 percent interest with no closing costs. This $10,000 (or the amount they decide on, usually up to a maximum of 80 percent of the assessed value of the home, including the first mortgage) is then available to be used in the acquisition of other real estate.

◀ *Technique 29:*
Refinance Boat, Car, Stereo

It is often worthwhile to refinance personal property that has considerable equity in order to quickly raise capital to take advantage of excellent investment opportunities.

2. Obtaining Long-term Loans from Hard-money Lenders

The first purchase that any investor in real estate needs to make is his own home. There are several types of loans available from government-sponsored sources that make it relatively easy for a person to finance his first home with a very small or in some cases no down payment.

Technique 30: ▶
VA Loans

30

For American investors or others who may be investing in the United States, it is important to understand VA loans. The Veteran's Administration in the United States has made it possible for veterans of the U.S. armed services to buy a property without having to make any down payment. It's a 100 percent loan; the only cost involved would be some minor closing costs which may amount to perhaps 1 percent of the purchase price. These loans are always available, in either tight or loose money markets. The interest rates are generally slightly lower than the prevailing market rates. The only disadvantage is that the seller of the property has to pay what we call points. Points are costs that the lender charges the seller of the property on the front end to compensate for giving him a lower interest rate. If a bank is charging three points on a loan, this would mean 3 percent of $50,000, which is $1,500 as a closing cost. This is not usually well received by all sellers, but in most instances the seller can go along with a VA loan if they can raise their price to cover the cost. So this way the buyer ends up paying the cost indirectly.

VA loans are generally harder to get initially for the initial borrower because of the red tape and government paper work that has to be filtered through in order to get the loan qualified. In addition, the Veteran's Administration is very picky about the kind of properties they like to lend on, and they also require certain kinds of improvements on the properties that are being purchased to bring them up to standards of the Veteran's Administration.

Although the loans are relatively more difficult to obtain in terms of the paper work involved, *it is very easy for a buyer of a property that has been previously financed with a VA loan to assume that loan and to take over the payments.* There are generally no qualifications whatsoever, and it only requires the payment of a small assumption fee and a very simple form to fill out. Therefore, as you are looking for properties to purchase, to assume a Veteran's Administration loan is a very good idea.

31

Technique 31: ▶
FHA Loans
(In Canada, CMHC)

The next technique is using FHA Owner Occupied Mortgages (CMHC in Canada). The Federal Home Administration in the United States (Central Mortgage and Housing Corporation in Canada) has several programs available to help the average person get into a home with a very small down payment. In some cases this is as little as 5 percent and even lower. The same kinds of policies are inherent with this type mortgages as with VA mortgages: there are points for the seller to pay, the paperwork is more difficult, and the appraisals, which are done by the FHA (or CMHC), are generally very conservative. However, like the VA mortgage, an FHA (or CMHC) is very easy to assume. They don't require any difficult paper work.

1. Note on Occupancy Requirement for These Loans

In the next section we will be discussing ways of using non-owner occupied loans to obtain little or no down payment transactions. Generally speaking, most of you have already purchased your first home and therefore are not eligible for all of the lower-down-payment, owner-occupied, available loans. As an investor, you just cannot legally or honestly apply for an owner-occupied loan and then not move into a home. If you are planning to use an owner-occupied loan, then move into that property and live in it. There is at this present time no legal limit for requiring a purchaser to *stay* in his property for a specified amount of time before he vacates the property. However, it has been my position that I do not attempt to obtain a low-down-payment, owner-occupied loan for the purpose of saving myself a down payment without eventually planning to live in that property. Many other individuals bend this rule, and because of this the FHA (or CMHC) and other institutions have been taking a closer look at who the people are who are borrowing the funds. In many cases they may monitor your mailboxes

for a period of several months after the transaction to make sure that you're actually occupying the home that you said you were going to occupy.

In one of these instances (in this case involving an FHA arrangement), one of my students purchased five owner-occupied homes in one month from five separate lending institutions, telling each of them that she and her husband were planning to move into these properties. This is neither wise nor safe. In this case the FHA became aware of her activities and threatened to take legal action if she did not divest herself of these properties immediately. And she became an immediate don't wanter. Be careful and be honest.

32

◀ *Technique 32:*
The Second Mortgage Crank

1. Understanding the Backgrounds: Conventional and FHA (or CMHC) Non-Owner Occupied Loans

The type of loan that you will be predominately involved with is the conventional non-owner occupied loan or an FHA (or CMHC) non-owner occupied loan. Both of these loans are created for investors, people who are not planning to occupy their property but are planning to rent it out. In most cases the buyer is required to make a 25 percent down payment on the property, and the lending institution will lend the borrower or the buyer up to 75 percent of the value of the property according to their appraisal. In times of tight money the conventional non-owner occupied loans which you normally can obtain from most savings and loan institutions are nonexistent. This is the first money to dry out when we are having a short period of tight mortgage money. In periods of very loose mortgage money, this conventional non-owner occupied loan is one of the easiest to get because the lending institutions are trying very seriously to loan out as much money as they possibly can; and therefore, when we have a very loose money market, you should concentrate in conventional non-owner occupied loans.

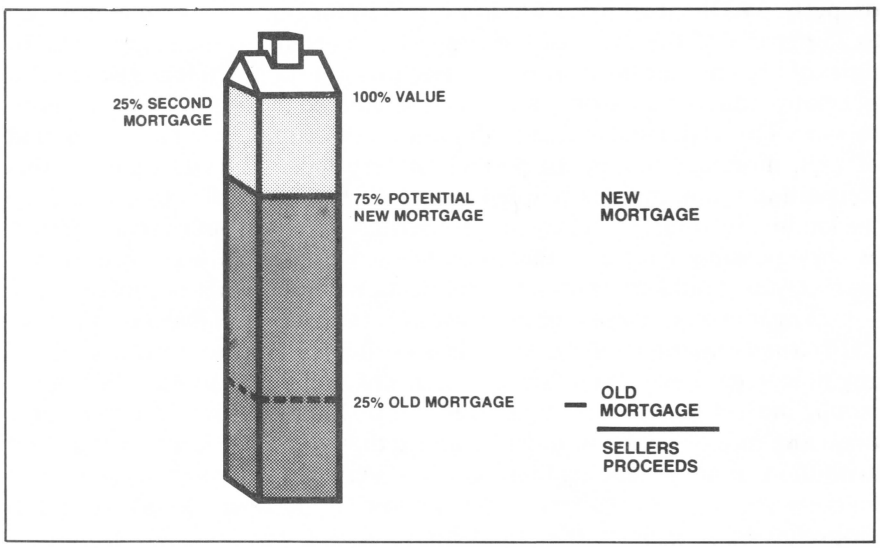
In tight money markets the only type of loan that is available is an FHA (or CMHC) non-owner occupied loan. This is available in any area, in any city, at any time, regardless of the financial status of the money market. When the money market is extremely tight, this will be the only source of long-term financing money, and you must be aware that you must learn how to find institutions that are making these kinds of loans. In extremely loose money markets you can use conventional non-owner occupied loans to obtain properties in sizes from the small house all the way to a 20- or 30-unit apartment building. But in extremely tight money times, the only types of properties that can be readily financed are properties that can qualify for government non-owner occupied loans. And this is generally only up to four-unit apartment buildings.

If we know that we can use a government non-owner occupied loan at any time, it opens up to us the opportunity to make a nothing down purchase. At this present time, for example, the FHA is permitting a real estate investor to borrow up to 85 percent of the normal amount of a regular FHA owner occupied loan. This usually works out to a loan equal to about 80 percent of the value of the property, i.e., somewhere between 80 and 82 percent of the value of the property can be borrowed, depending on the FHA appraiser. This 80 percent loan-to-value ratio is sometimes lowered if the property rent is low. If rents are really low in your area, you may only be able to obtain a 60 to 70 percent loan through FHA (or CMHC). Check out these details before you make your offer so that you are prepared. The government-appointed appraiser will come in to appraise the property at a certain figure, and the government will guarantee a loan of approximately 80 percent of the value of that appraisal, depending on the property rental picture. You must be aware of the FHA (CMHC in Canada) and know that they are notorious for being conservative, which means that they generally appraise low. In

your offers to purchase properties, you might make allowances for the differences of appraisals by these government people. In some instances the amount of your appraisal is very critical for you to be able to buy the property with a nothing down transaction. You should put in a clause making the transaction subject to the property being appraised at a certain figure by the appraiser, or you may be forced to come up with money out of your pocket. It is also possible to influence the appraiser by showing him other properties that seem to be comparable with the price of yours. Once you know this information, you can begin to look for properties that may seem to lend themselves to a technique which I call the second mortgage crank.

2. Details of the Second Mortgage Crank

The second mortgage crank is very powerful if you can locate a property that has an existing loan of less than, say, 25 percent of the property's current value. If the seller will be flexible in the way he receives his equity and does not require that you pay him all his equity in cash, then you can increase the probability of buying the property with absolutely none of your own money. Look at the following example:



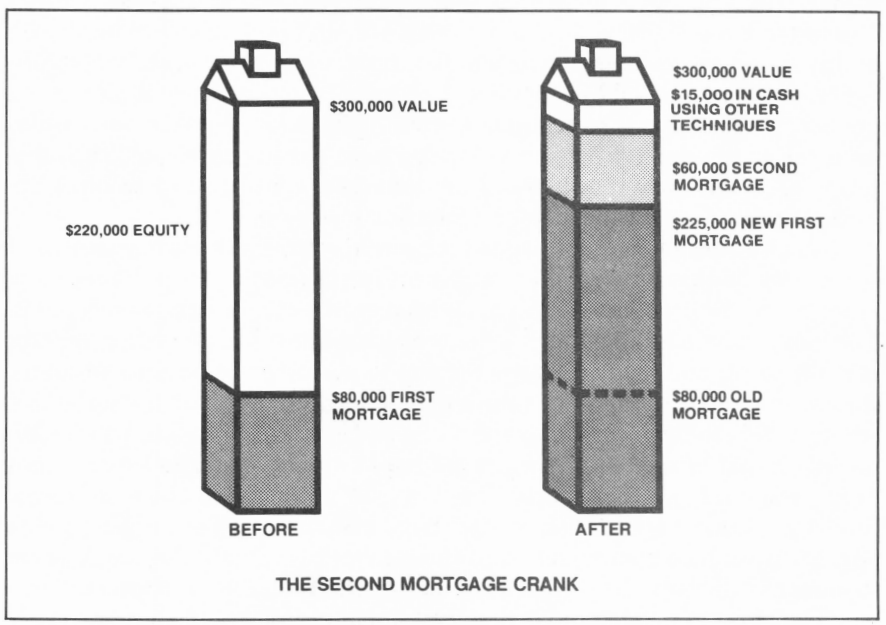
Here we have a property with a 100 percent value and a 25 percent old mortgage. If I know that I can obtain approximately a 75 percent potential new mortgage, then I know that the difference between the new mortgage and the old mortgage equals the seller's proceeds. In other words, the difference between those two mortgages is cash that can be paid to the seller at the time of the closing. If the seller will be satisfied to accept that cash as the only cash he receives from the sale of a property and in addition will take back a second mortgage for the rest of his equity, which is secured above the brand new first mortgage, then I have just negotiated a nothing down transaction. I am in essence borrowing my down payment by refinancing the property and giving the seller the difference between the two mortgages in cash. This technique is particularly powerful when the following ingredients are available: (1) When I find an anxious seller who needs some cash but is willing to be flexible with a portion of his equity. (2) When I can find a mortgage low in relationship to the property value, less than 50 percent (preferably under 25 percent); in other words, the seller has a lot of equity. (3) If there is a loose money market. (4) If there is a tight money market and I have the ability to qualify for a mortgage loan or am able to find a partner who is able to qualify.

This technique is especially good when real estate agents are involved because there is usually plenty of money for the seller to pay a real estate commission. The seller gets cash, the real estate agent gets cash, and the buyer still ends up with a nothing down transaction. The only thing that is important to be careful about at this point is to check through the mortgages so that there are no negative cash flows that you cannot handle. Let's take a look at a specific example of a second mortgage crank and show you how it can be used to buy small or large properties.

3. A Case History

My first second mortgage crank property was a 12-unit building. I located a seller who had a $300,000 property with an existing $80,000 first mortgage. He had $220,000 in equity. The seller was inflexible in his price, and at that time the price was actually just a little bit high. But he was flexible in the way he would receive his money. I knew that if I could obtain a brand new first mortgage on the property of $225,000, which was at that time 75 percent of the value of the property, that the difference between the new first mortgage of $225,000 and the old mortgage of $80,000 would leave $145,000 in cash, which would be given to the seller at the time of the closing. This $145,000 in cash was a very large amount of money that the seller was receiving, and I knew that if I could just convince the seller to take back a $75,000 second mortgage, in other words have him take $145,000 in cash and $75,000 in the form of a second mortgage, that I could buy that property with absolutely nothing down out of my own pocket.

The seller reviewed my offer and said that he would not take the $75,000 second mortgage but would only carry it at $60,000. That meant that I was $15,000 short, which I had to come up with out of my own pocket. I knew that by using one of the other techniques we learned earlier, for example, using the rents and deposits, that there would be some funds there to apply towards the $15,000. So I proceeded to make the offer and to try to obtain my financing. The chart shows the plan graphically.



THE SECOND MORTGAGE CRANK

There were several hurdles that I had to overcome. The first hurdle was that I had to be able to locate non-owner occupied or investor mortgage money, and luckily we had just come out of a tight money situation, and the mortgage funds were plentiful. The second problem was that I had to be able to qualify for a brand new $225,000 first mortgage, and at that time, since my

annual income was about $20,000 to $25,000 less than needed, I was not eligible to qualify for that new loan. So I approached a friend and offered him a half interest in the property if he would come with me and go in on the purchase and let me co-sign on the property. That way we could be strong enough together to obtain that new loan. He agreed to come in with me, since he did not have to come up with any money of his own.

The next problem was that I had to be able to obtain the $15,000 in down payment. The property itself was a 12-unit apartment building rented out to students, six students in each apartment, 72 girls. They had to pay first and last month's rent when they moved in, plus a deposit of $80.00 per girl. The first and last month's rent at $70.00 per girl came to almost $10,000, and the deposits themselves came to just over $5,000. Therefore, a total of $15,000 was waiting for me in a special bank account on the day that I would take possession of the property, and that $15,000 was used as the remaining portion of the down payment that was necessary for me to be able to buy this property. (I should interject parenthetically that legislation in some states and provinces may prohibit putting deposit monies to this type use—so check carefully in your area!) The closing costs themselves were somewhere in the neighborhood of $5,000, and my partner and I went down to a bank and borrowed the $5,000 on a short-term note to complete the transaction.

The next problem arose when I had to make sure that this property appraised for $300,000. If it were appraised for anything less than that, I would have to come up with money out of my pocket. So I immediately called up the appraiser and had a long chat with him. I shared with him the addresses and the recent sales prices of many of the higher-priced apartment buildings in the area to verify that the property should sell for at least $300,000. Luckily the appraisal came to $300,000 without the furniture. One of the other problems I faced was that the seller wanted a $5,000 down payment in cash to be held as a deposit in case I didn't go through with the transaction, because he did not want to tie the property up without having some action. So once again that was a problem for me because I didn't happen to have $5,000 sitting in my bank account. So I gave him an option on my first duplex which stated that if I didn't close the transaction within the six-month time that I negotiated, then I would give him my duplex as the down payment. He was reluctant but agreed to it, and it seemed to satisfy him for a period of time. I realized that I took a large risk in being able to buy this property, but I knew that it could be done and I just needed to burn my bridges behind me so that the pressure was really on.

The next problem that I had to face was how to obtain the loan from the bank if the bank was aware that I was investing none of my own money. This is a very touchy problem and becomes even more acute in tight money times. The banks have a habit of turning their heads a little bit if the money market is really loose, and they are under the gun to place a great number of loans. But when the money market is extremely tight, then everyone tightens their scrutiny of even the most minor parts of a real estate transaction. The reason for this is that in tight money times the banks and savings and loans do not keep these loans in their portfolios. They do not use their own investors' funds but rather borrow money from large investors such as pension funds and life insurance companies. And these investors are usually much more stringent in the way they lend their money and much more conservative.

The point to understand is that the banker is concerned about two very important aspects of a non-owner occupied loan. (1) His concern is the question, "Where is your down payment? Can you verify that you have made a down payment on this property or that you will be making a down payment on the property?" (2) The second concern is, "Have you borrowed the down payment to buy this property?" This becomes even more critical when you

D. NAME OF BORROWER:	E. NAME OF SELLER:	F. NAME OF LENDER:
Robert G. Allen		XYZ Bank
G. PROPERTY LOCATION:	**H. SETTLEMENT AGENT:**	**I. SETTLEMENT DATE:**
751 Vista Lane	XYZ Bank	1-13-77
	PLACE OF SETTLEMENT: Orem, Utah	

J. SUMMARY OF BORROWER'S TRANSACTION		K. SUMMARY OF SELLER'S TRANSACTION	
100. GROSS AMOUNT DUE FROM BORROWER:		400. GROSS AMOUNT DUE TO SELLER:	
101. Contract sales price	$ 300,000.00	401. Contract sales price	$ 300,000.00
102. Personal property		402. Personal property	
103. Settlement charges to borrower *(line 1400)*	7,073.81	403.	
104.		404.	
105.		405.	
Adjustments for items paid by seller in advance		*Adjustments for items paid by seller in advance*	
106. City/town taxes to		406. City/town taxes to	
107. County taxes to		407. County taxes to	
108. Assessments to		408. Assessments to	
109.		409.	
110.		410.	
111.		411.	
112.		412.	
120. GROSS AMOUNT DUE FROM BORROWER	307,073.81	420. GROSS AMOUNT DUE TO SELLER	300,000.00
200. AMOUNTS PAID BY OR IN BEHALF OF BORROWER:		500. REDUCTIONS IN AMOUNT DUE TO SELLER:	
201. Deposit or earnest money	5,000.00	501. Excess deposit *(see instructions)*	
202. Principal amount of new loan(s)	225,000.00	502. Settlement charges to seller *(line 1400)*	993.00
203. Existing loan(s) taken subject to		503. Existing loan(s) taken subject to	
204. Note to seller	60,000.00	504. Payoff of first mortgage loan	
205.		505. Payoff of second mortgage loan	
206.		506. Earnest Money	5,000.00
207.		507. Western Mortage Loan Corp.	82,398.02
208.		508. Note from borrower	60,000.00
209.		509. Credit Union	2,944.31
Adjustments for items unpaid by seller		*Adjustments for items unpaid by seller*	
210. City/town taxes to		510. City/town taxes to	
211. County taxes to	240.00	511. County taxes to	240.00
212. Assessments to		512. Assessments to	
213.		513.	
214.		514.	
215.		515.	
216.		516.	
217.		517.	
218.		518.	
219.		519.	
220. TOTAL PAID BY/FOR BORROWER	$ 290,240.00	520. TOTAL REDUCTION AMOUNT DUE SELLER	$ 151,575.33
300. CASH AT SETTLEMENT FROM/TO BORROWER		600. CASH AT SETTLEMENT TO/FROM SELLER	
301. Gross amount due from borrower *(line 120)*	$ 307,073.81	601. Gross amount due to seller *(line 420)*	$ 300,000.00
302. Less amounts paid by/for borrower *(line 220)*	290,240.00	602. Less reductions in amount due seller *(line 520)*	151,575.33
303. CASH (☒ FROM) (☐ TO) BORROWER	$ 16,833.81	603. CASH (☒ TO) (☐ FROM) SELLER	$ 148,424.67

Federal National Mortgage Association

REQUEST FOR VERIFICATION OF DEPOSIT

INSTRUCTIONS: LENDER - *Complete Items 1 thru 8. Have applicant(s) complete Item 9. Forward directly to depository named in Item 1.*

DEPOSITORY - *Please complete Items 10 thru 15 and return DIRECTLY to lender named in Item 2.*

PART I - REQUEST

1. TO *(Name and address of depository)*	2. FROM *(Name and address of lender)*

3. SIGNATURE OF LENDER	4. TITLE	5. DATE	6. LENDER'S NUMBER *(Optional)*

7. INFORMATION TO BE VERIFIED

TYPE OF ACCOUNT	ACCOUNT IN NAME OF	ACCOUNT NUMBER	BALANCE
			$
			$
			$
			$

TO DEPOSITORY: *I have applied for a mortgage loan and stated in my financial statement that the balance on deposit with you is as shown above. You are authorized to verify this information and to supply the lender identified above with the information requested in Items 10 thru 12. Your response is solely a matter of courtesy for which no responsibility is attached to your institution or any of your officers.*

8. NAME AND ADDRESS OF APPLICANT(s)	9. SIGNATURE OF APPLICANT(s)

TO BE COMPLETED BY DEPOSITORY

PART II - VERIFICATION OF DEPOSITORY

10. DEPOSIT ACCOUNTS OF APPLICANT(s)

TYPE OF ACCOUNT	ACCOUNT NUMBER	CURRENT BALANCE	AVERAGE BALANCE FOR PREVIOUS TWO MONTHS	DATE OPENED
		$	$	
		$	$	
		$	$	
		$	$	

11. LOANS OUTSTANDING TO APPLICANT(s)

LOAN NUMBER	DATE OF LOAN	ORIGINAL AMOUNT	CURRENT BALANCE	INSTALLMENTS *(Monthly/Quarterly)*	SECURED BY	NUMBER OF LATE PAYMENTS
		$	$	$ per		
		$	$	$ per		
		$	$	$ per		

12. ADDITIONAL INFORMATION WHICH MAY BE OF ASSISTANCE IN DETERMINATION OF CREDIT WORTHINESS:
(Please include information on loans paid-in-full as in Item 11 above)

Subject to the requirements of the Fair Credit Reporting Act, the information provided in Items 10 thru 12 is furnished to you in strict confidence in response to your request. The accuracy of such information is not guaranteed.

13. SIGNATURE OF DEPOSITORY	14. TITLE	15. DATE

This form is to be transmitted directly to the lender and is not to be transmitted through the applicant or any other party.

get FHA (or CMHC) non-owner occupied loans where the forms that you fill out call for you to state that you have not borrowed any part of this down payment. "Is there any secondary financing?" is the major concern. And in our example there is secondary financing; I have borrowed a portion of the down payment. Since this was my first transaction, I did not realize that these were major concerns of the bank, and the banker pointed out to me that I did not have any down payment in the property but that he was going to go ahead and make the loan anyway because they were in a very loose money market, and they wanted to place as many loans as they possibly could. He pointed out to me that in a tight money situation he would not be permitted to make that kind of loan. I have since come up with several solutions to solve this particular problem as far as a non-owner occupied borrower is concerned, and those solutions are given below.

Of course, in any transaction of this type that you as an investor may structure, it is essential to get the best professional advice in regard to current practices and legislation that may have a bearing on the transaction. The main point I want to make is that careful planning and thinking will in most cases lead to creative solutions acceptable to all parties concerned.

4. A Further Example

Let's take an example here that can help us in trying to determine how to obtain a non-owner occupied loan with no down payment. Suppose we located a $50,000 house which has a $20,000 existing mortgage on it. The seller has $30,000 of equity and does not want to receive all of his equity in cash and is willing to take back a certain small portion as a second mortgage with a monthly payment attached to it. And so we go down and check with FHA non-owner occupied loans (in Canada CMHC), and we find that we can obtain an 80 percent loan on the value of that property. We have it appraised at $50,000, and we know that we can obtain an 80 percent loan on the value of that property, which would be approximately $40,000. We make application for the loan, knowing that when we take the loan of $40,000 on the property, the difference between the $40,000 and the $20,000 existing mortgage is $20,000. That amount of money will be paid to the seller in cash. The seller, therefore, receives $20,000 of his $30,000 equity in cash. The remaining $10,000 is taken out in the form of a second mortgage, which will be placed upon the property that you are buying. The FHA (or CMHC) is extremely concerned that if the seller takes back his $10,000 second mortgage, then you are borrowing a portion of your down payment, and there is secondary financing on that property that you are buying, which may not be acceptable under the loan provisions at the bank. Since this is going to be a major concern of the lender, we are going to have to be able to alleviate those concerns by doing one of the following several actions.

5. Alleviating the Fears of the Lenders

a. Creating Paper and Moving the Mortgage. In an earlier section we talked about the creation of paper, that is, creating a note against the equity in your own piece of property to secure a down payment on another. This is a very important technique with respect to the second mortgage crank. Our seller in this case is going to get $20,000 in cash. He still is going to receive a $10,000 secured second mortgage, and if we can convince him that he is going to be equally as secured on your own home as he would have been in receiving security on the property he is selling, then we virtually solve our problem with the lender. We must be able to convince the seller that his $10,000 note is going to be paid back and that the only concern he should have is that his $10,000 should be secured against an adequate piece of property. If you do have that piece of property, such as your own home or another particular

piece of property you own, you can convince him to take a second mortgage against it. And this is done very simply by giving him a trust deed for $10,000 against another piece of property.

Then we can go into the lender to ask for a loan. The lender asks you, "Is there any secondary financing on this piece of property?" You can answer in all honesty that there is not. In reality the second mortgage has been transferred to another piece of property which is another piece of security. Now the lender may want some proof of this, and you may have to provide him with that proof by showing him that you have given the seller a trust deed and a trust deed note against another piece of property.

Or you may not even share that information with the lender but tell him that you have already given the down payment to the seller in the form of an exchange in consideration for the seller's equity of $10,000 and that you can verify this by having the seller sign a document that is called a verification of deposit, and this verification of deposit states that the seller has already received consideration for his equity in the form of an exchange. This should satisfy the demands of the lender. The lender, of course, will realize that the property that you are buying does not have additional secondary financing on it, and he will look to your capacity to repay the second mortgage secured by your own piece of property. In your financial statement that you prepare for the lender, you will probably have to show that there is an additional second mortgage on your own piece of property. If you admitted this and did not show this to a lender, then he may be justified in saying that you are fraudulently trying to obtain a loan.

The basic ingredients for this moving of the mortgage technique or the creation of paper is that you convince the seller (a) that he should move his mortgage or move his security to another piece of property that is adequately secured and (b) that you convince the lender that his property will not be held in jeopardy because you are actually using other property as the down payment, and this should satisfy his demands. Now there is nothing to say that once the transaction has been completed you could not once again resubstitute collateral for the amount of that $10,000 note and move the mortgage from your own home back onto the house you are buying after a period of two or three months. The lender is just concerned in the initial stages that you are not highly leveraging yourself into a piece of property. He is concerned about his own security.

b. An Alternative: Moving the Mortgage to a Partner's Property. Those of you who do not have a piece of property to move a mortgage to have the additional alternative of finding a relative or friend or partner to come in and participate in the purchase of this piece of property by letting you move the $10,000 mortgage from the purchased property onto your partner's property, and that could be the contribution that your partner makes to the purchase. If you don't have the ability to qualify for a loan, you can also get your partner to qualify for the loan for you.

c. Personal Note Method. If neither one of these alternatives seems to be open to you, you could try another solution and that is have the seller accept a personal note for the remaining $10,000. Since there is no security involved in a personal note, the seller might accept $20,000 in cash and a $10,000 personal-unsecured note with terms arranged between you.

d. The Contract of Sale Method. If none of those alternatives seems to be available to you, you may have to resort to the following approach called the contract of sale method. In this method you arrange to purchase the property from the seller with a very small down payment, perhaps $1,000 now. In our

example of this $50,000 house where the seller has the $30,000 equity, we agree to give him $1,000 now with $19,000 coming in six months, and the remaining $10,000 which is still owed is paid on the basis of the next several years. Then we buy the property from the seller on a contract of sale, also called a wrap-around mortgage. If that's the case, we find ourselves in the position of being an owner of the property. The bank is not going to ask us any questions such as, "Is there any secondary financing on this piece of property for the purchase?" or "What is your down payment?" etc. They will only be asking you questions like, "Are you able to borrow the money? What is the value of the property?" and then you make the application for the refinance.

This method will only work well if you plan to improve the value of the property significantly before you refinance the property, otherwise the bank will check the title policy and see that the new loan will not be enough to pay off the existing indebtedness. This will cause the banker to wonder about the whole transaction.

e. The Temporary Use of Cash Accounts. One last possible way of convincing the banker that he should lend on a second mortgage crank is that you could have your $10,000 cash down payment in your bank account, and when the banker asks you where the down payment is, you could say, "The down payment is in my bank account and will be handled as normal." The banker therefore assumes that when you refinance this piece of property, you're going to put a $10,000 cash down payment and refinance a $40,000 loan. In essence what you're planning to do is to use your $10,000 down payment at the beginning stages of the purchase, and as soon as the property is refinanced and the seller receives your $10,000 in cash, then you have him lend that money back to you after the fact. You make arrangements for him to keep the $10,000 in a separate escrow account for a few days and then have a title company arrange for you to receive the $10,000 back and substitute in its place a $10,000 second mortgage secured by the property that you're buying. The loan officer may frown upon this alternative if he were to know the whole story. It must be used carefully and only if you have indication that the banker feels it is all right.

A variation of this approach which I recently have become aware of is this: A fellow in Los Angeles was mentioning that he just borrows $10,000 from his mother and places it in a bank account. Then when the bank verifies that the $10,000 is there, he just gives the money back to his mother, and the bank thinks that the $10,000 is going to be used for the down payment, but it never really changes hands. That's a little devious, and I would not recommend it, but I mention it just to let you know that there are other ways of skinning a cat. With some thought and planning, you may be able to develop alternative solutions that would be acceptable to all parties concerned.

f. Summary. Inherent in the above discussion is the understanding that each savings and loan company has different guidelines about the requirement of down payments. If we find a loan officer who gives us a hard time about the details of a transaction, we may just need to transfer the loan papers to another, more receptive lending institution. And once we find a great, easy-to-work-with loan officer, we treat him like gold.

Needless to say, this second mortgage crank technique is an extremely powerful one because it combines many of the creative financing techniques that we have talked about previously without having to look for a serious don't wanter. Most sellers are amenable to receiving a major portion of their cash at the closing and have already been trained to think that carrying back

a second mortgage of some amount may not be all that bad. The way to locate these kinds of transactions is through your multiple listing book. This is an excellent source of second mortgage cranks because it frequently lists the mortgages and the sales price and whether or not the seller is willing to carry back some paper. All you need to do is look for a property that has a low mortgage and a high value where the seller is willing to carry back some paper and make him an offer on the second mortgage crank and proceed from that point to buy the piece of property.

In one two-month period of time here recently, a partner and I purchased three homes this way—one right after the other from the same lending institution. These kinds of properties exist, and the only real major problem is the structuring of the mortgages so that there are no negative cash flows. We discussed how to do this in Section K.

Technique 33: ▶
Variation of the Crank:
Seller Refinance

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Note this additional twist on the second mortgage crank: You could give the seller an extra $1,000 and have him go down to the bank and have him qualify to refinance his own piece of property and then sell it to you on the terms as previously specified. If the seller were to do this, the mortgage would be in the seller's name, but once the refinance was completed, you could go in then and assume the mortgage from him. Once the property was refinanced by the seller there would not be any questions from the banker like, "Where is your down payment?" or other such questions. Now there are problems with that. What's to stop the seller from saying, "Well, if I'm going to refinance my own piece of property, why shouldn't I just keep it?" Well, that's something that has to be negotiated, and some sellers are going to be that way, and others aren't; it's just a matter of individuality between you and your seller.

Two of our graduates from Tucson, Arizona, bought some $2 million worth of single family homes in a year's time recently, using the second mortgage crank technique. Of these nearly 40 properties, around one-third were purchased by having the seller refinance in his own name—in this case put a new second on the house—prior to the buyers taking over the property. Their formula was this: find a property with a fairly small, low-interest, fully-assumable first mortgage. Put on a new hard-money second (or have the seller do this and then assume it). Have the seller carry back the balance of his equity in the form of a third with a single-payment note due after seven years at around 12 percent. Cash flows are never more than $100 negative per month. Only one or two of the sellers who were asked to put on a second in their name decided not to sell when taught this technique.

Technique 34: ▶
Buy Low, Refinance High

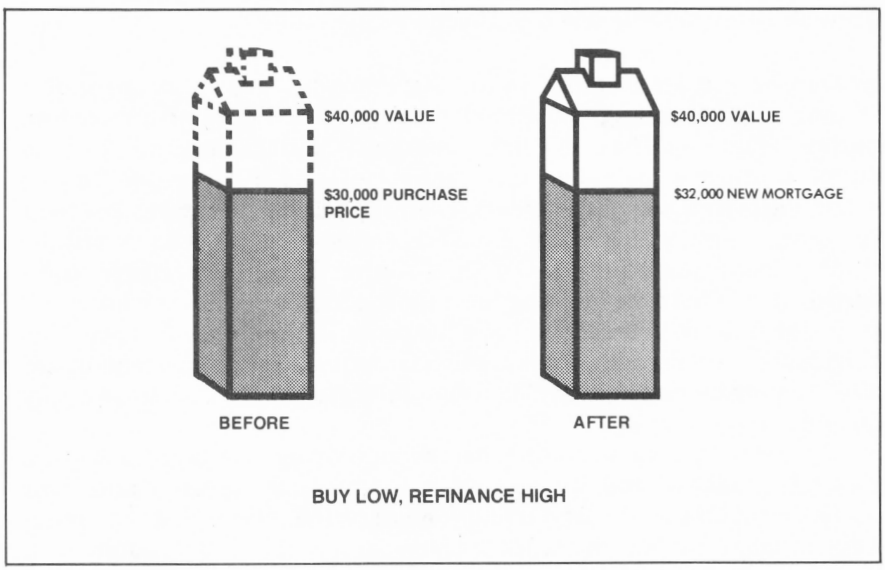
34

Now the next section that we're going to discuss is the Buy Low, Refinance High Technique. This technique requires an extremely good knowledge of the marketplace and in most cases the ability to come up with large amounts of money in a short period of time for a short-term loan. Now for those of you who are fortunate enough to have large amounts of cash in your savings account, one of the most valuable techniques that I can explain to you is this Buy Low, Refinance High Technique. Let's make two assumptions. The first assumption is that you have, say, $30,000 cash in your bank account now and that it is idle and waiting to be invested in a piece of property. Your first step would be to go into the marketplace and understand the money market. Find out where there are existing non-owner occupied loans and discuss with the bankers and lending officers of these banks the requirements to obtain a non-owner occupied loan and the time frame and the interest rates, etc. The next step is either to place an ad in the paper which advertises that you will pay cash in a 24-hour period of time for those people who are willing to substantially discount the equity of their property. Then you notify your

agents that you are looking for an individual who either does not understand the value of his property or who is willing to substantially discount the value of his property if he could receive cash within an extremely short period of time.

1. An Example

Let's take an example. Suppose we go out into the marketplace, and we locate ourselves a property which is worth approximately $40,000, and the seller either does not realize the value of it or is willing to discount or sell the property for $30,000 cash immediately. See the illustration following. We are looking for property that either in its present state is worth more than the seller is asking for or could be perhaps painted and touched up to make it look more valuable than its current value. We come in, and we buy the property with our $30,000 down payment in cash. We now are the legal and rightful owners of that property. Now we go to our non-owner occupied lending institutions, and we make application for a government-insured non-owner occupied loan (FHA in the U.S. or CMHC in Canada), which in this case will give us an 80 percent loan. Eighty percent of its appraised value of $40,000 would give us a $32,000 loan. This $32,000 loan would be enough money to completely refinance the house, returning all of our closing costs and our initial down payment and gives us the opportunity to buy a piece of property significantly below the market. We rent this property out for enough money to make the mortgage payments, we put it in our portfolio, and we now still have our $30,000 amount of money in our savings account, still waiting to be invested in another piece of property. Now this technique does not lend itself to being used very frequently, maybe once or twice or three times a year, but for most investors two or three times a year is more than adequate to take them to financial independence in a five- to 10-year period of time.



2. Using Partners

For those of you who do not have $30,000 or $40,000 cash lying around in your bank accounts, you may be able to use our bank-lending technique for borrowing funds from short-term lenders, or you might use a technique (discussed below) of using a partner and bring the partners together to come up with a down payment.

The power of this technique is that it is possible to use your money and to roll that money three or four times in three or four different investment pieces of property without even having to touch your initial capital. It's only used for a short period of time, then it's refinanced out again, and it's used again, and it's refinanced out again, and it's used again, and it's refinanced out again. It's a very powerful technique and should not be overlooked for those people who have the amount of money to devote to this type of an activity.

Some of you have seriously considered refinancing your own homes to generate cash for your investment program. I highly recommend this technique for that avenue of investments for the beginning investor. It not only provides you an immediate profit, but it gets all of your cash back into your pocket for an additional investment. Your money doesn't have to be invested on a long-term basis, and it is a very conservative technique because in the eventuality that there is any trouble with the economy, you will have enough lead time to refinance your money out and put your money into safer investments.

So with that discussion we are now going to leave our use of long-term mortgages, and we are going to be talking about the flexibilities of holders of underlying mortgages.

G. HOLDERS OF UNDERLYING MORTGAGES

One of the most important questions that we ask the seller as we're doing our preliminary fact finding is "How many mortgages are there on your property?" and "Who is the holder of each of the mortgages?" Banks are usually not flexible with their dealings on underlying mortgages. But in many cases the properties that you're buying have been financed by private lenders, private individuals, or previous owners of the same property who carried back paper when they sold their property. This offers a very interesting opportunity for nothing down transactions.

Technique 35: ▶ Use Discounts from Holders of Mortgages

35

Let me give you an example. In the diagram you have an example of a building which is selling for $80,000. Perhaps it's a duplex or a three-unit apartment building. The equity in the building is $20,000; there is an existing $60,000 contract of sale, and this contract of sale is to be paid to two underlying private mortgage holders. There is a $30,000 first mortgage at 6 or 7 percent interest, which is being paid to an older couple who owned the building many years previous to that. Above that is a mortgage to an individual who held the building for a short period of time but who sold it and made a profit and carried back his profit in the form of paper. This individual has a 9 percent contract, and he receives monthly payments on his $30,000 equity in the property. The seller of the property has a $20,000 equity which he wants in cash.

Our first step is to determine that the underlying mortgage holders are private individuals, and we may wish to do some research into their particular circumstances. And doing some research reveals that the underlying mortgage holders, the older couple who had the $30,000 equity with monthly payments of 6 to 7 percent interest (perhaps $250 a month), had once thought that the $250 a month would be adequate to supplement their retirement income. However, they are very worried about it. They have tried several times to sell their underlying contract but did not know how to go about getting cash for it. They find themselves with perhaps another 10 good years left together and with the possibility of having to live that 10 years together in virtual poverty. The fellow who owns the $30,000 equity above the private first also finds himself in a certain problem because his wife divorced him, and he is splitting their monthly payment of $250 a month—with him

receiving $125 and her receiving $125 a month. It really does not cause much of a dent in their monthly bills, and both of them would welcome an opportunity to receive cash and to liquidate this last joint asset remaining between them.

We might approach the individuals involved here and make them an offer. We state to them that we will give each of them $20,000 in cash within a six-month period of time if they will relinquish to us their interest in the aforedescribed property. The older couple faces the alternative of receiving $250 a month for a long period of time or receiving $20,000 cash now. This opens up new avenues to them. It gives them hope. Perhaps they can use the $20,000 to do some traveling they have always wanted to do. Perhaps they could live in a little bit better style and enjoy the last remaining years of life. They may be very interested in taking a discount in the value of their mortgage now for the opportunity of having cash. The same goes for our divorced couple. Each ex-spouse would receive approximately $10,000 in cash. They could go on their way and not have to worry about one another any longer.

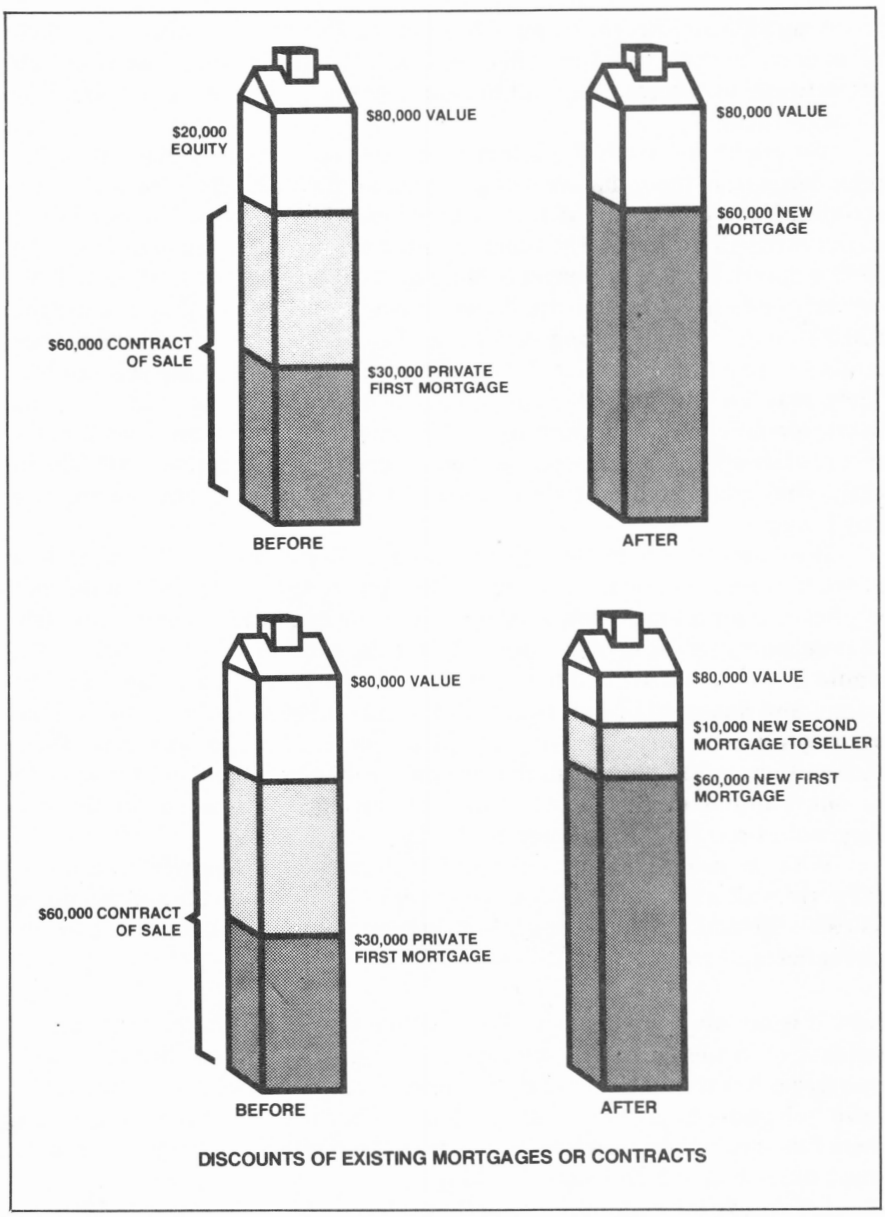
If we were able to negotiate this kind of discount for the mortgages, this is what would happen. We would next go to the bank and make out application for a brand new $60,000 first mortgage, which is approximately 75 percent of the value of the property. Of the $60,000 in cash, $20,000 of it would be immediately paid to the existing owner as his equity. He would be happy, and he would be out. Twenty thousand dollars would go to pay off the underlying first mortgage with the older couple. They would receive their money, they would relinquish their interest in the property, and they would be out. The remaining $20,000 would be paid to the divorced couple, and they would receive their money, and they would be out.

What we just accomplished is the purchase of an apartment building or property with absolutely no down payment and in the same process made $20,000! We could sell that same building on the marketplace immediately thereafter and collect our $20,000 profit.

1. Inducements

Now it is not always as neat as this example may indicate. Many times the holders of underlying first mortgages are not willing to discount their mortgages but would be more than happy to receive monthly payments. We have to be able to give them the kind of inducements that might convince them that it is in their best interest to either discount their mortgages or to do some other creative and sensible thing.

Let's make the assumption that the underlying first mortgage holder, the older couple in our previous example, would be willing to discount their mortgage, but the divorced couple would not. What could we offer the divorced couple that would facilitate our purchase and still let us get into this property with absolutely no cash out of our pocket? Perhaps we could offer them $20,000 in cash with a $10,000 new second mortgage on top of the existing brand new first mortgage of $60,000. In that way they would receive $20,000 in cash and $10,000 in mortgage payments with monthly payments still coming in. This mortgage could be either a personal note or a second mortgage secured by another piece of property you own. If you offer a mortgage holder cash with the opportunity of receiving the rest of it coming in monthly payments in the future, they should be rather flexible in the way they deal with you. Sometimes the amount of the privately-owned first mortgage is not enough to make an entire down payment, and only a portion of the down payment can come from discount, then you find yourself in a position of having to either borrow the rest of the down payment or to use the rents and deposits or to use partners or some other kind of technique which we have already previously discussed. The most important thing to



remember here, however, is that every time you inspect a piece of property you always ask what the situation is with respect to private mortgages.

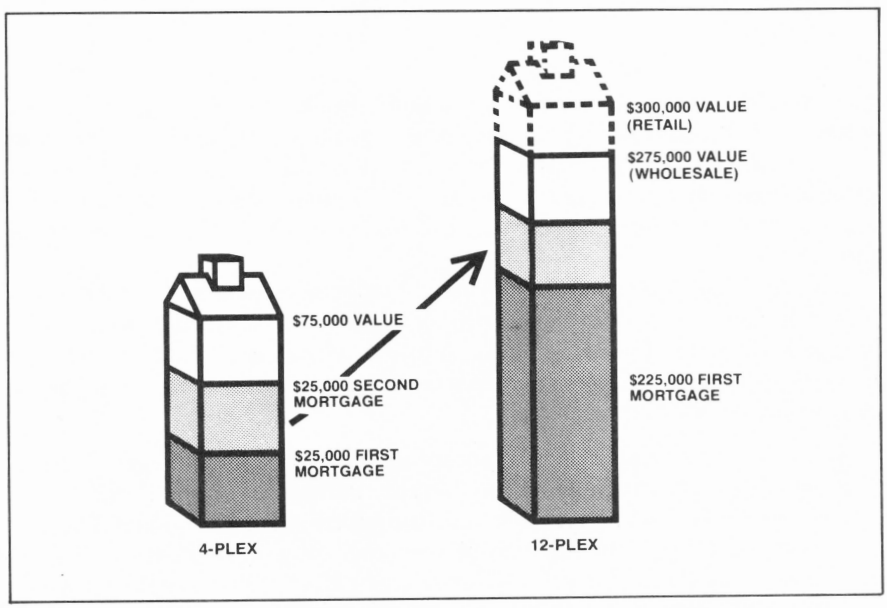
Technique 36: ▶
Moving the Mortgage

36

Now let's take another example of mortgages that are already being paid on an already existing property. A friend of mine approached me with a problem some time ago. And his problem was this. He had located a beautiful 12-unit apartment building with a retail value of $300,000. See the diagram included overleaf. The seller of the property, who had an existing $225,000 first mortgage, wanted a $50,000 down payment. My friend did not have $50,000 in cash. If he could obtain $50,000 in cash, he could buy the property, worth $300,000, for a purchase price of $275,000. He would make a $25,000 immediate equity profit the second he bought the property. I began asking questions about his assets. "What do you own?" Well, he owns a $75,000 four-unit apartment building with a $25,000 first mortgage and $25,000 second mortgage. His equity is $25,000. If he were able to sell his property, the only amount of cash he could raise would be $25,000, and he

would still be $25,000 short. Do you see in the information I've given you a possibility for him to be able to buy this property and make a profit without having to come up with money from his own pocket?

Your comments:



What we did in this example was to contact the holder of the $25,000 second mortgage, which was a private individual, to convince him that it would be in his best interest to release his mortgage on the four-unit

apartment building and take the brand new second mortgage on a larger, more valuable piece of property with an increase in the amount of collateral or security for a second mortgage. He was amenable to the move, and he agreed to move his mortgage to the 12-unit apartment building. This offered some very important opportunities for creative financing. If he were to agree to release his mortgage, we can thereby assume that his mortgage does not exist. My client or friend thereby arranged to sell his $75,000 four-unit apartment building to a person who was very interested in buying it and collected the entire $50,000 from the $75,000 value down to the $25,000 first mortgage. With this $50,000 in cash he went to the 12-unit apartment and gave that $50,000 as a down payment. Once that transaction was completed, the $25,000 second mortgage was moved from the four-plex to the 12-unit apartment building.

Now the mechanics of this are not complicated but need to be done in a very orderly fashion. The buyer of the four-unit apartment building enters the picture with a $50,000 cash down payment, and he makes his down payment to buy his four-unit apartment building. The only problem that exists there is that the second mortgage has to be released. Well, the closing agency (title company or legal firm) that is handling the transaction and acts as the third party here can do all the moving of the mortgages and all of the paper work necessary to make this transaction fall together without having to jeopardize anybody's interest. They have the second mortgage holder sign a "release of mortgage," thereby releasing the mortgage from the four-plex. They take the $50,000 from the buyer of the four-plex and give it to the seller of the 12-plex. The seller of the 12-plex gives the deed to the buyer of the 12-plex, my friend; he, therefore, executes a $25,000 second mortgage to the previous second mortgage holder, and everyone is happy. The buyer of the four-plex has his four-plex, the seller of his 12-plex has his $50,000 in cash, my friend has his 12-plex, and the holder of the second mortgage now has an increased amount of security. (Of course, a 1031 tax-deferred exchange could be completed by having the buyer buy the 12-plex in exchange for the four-plex [See Section R].)

1. Adding Some Sweeteners

Now you may have to sweeten the fellow's pocket by offering one of the following if he does not agree to want to move his mortgage: You can offer him an increased interest rate or a faster payoff of the loan or higher monthly payments or increased collateral. You can even offer him a certain amount of cash if he is willing to move his mortgage from one property to the next.

Suppose that you would like to be able to prepare yourself for the use of this technique but do not own a property at this present time. You should always include the following paragraph in any trust deed that you prepare for a property that you are buying where the seller agrees to carry back a second mortgage.

> "The seller hereby agrees to accept a substitution of collateral for the amount of this note by moving the mortgage (or trust deed) to another piece of property which the buyer shall designate. The seller shall have the right to inspect such property to insure the security of the collateral and shall give his approval to make the substitution of collateral . . . which approval shall not be unreasonably denied."

This paragraph I'm going to refer to as the substitution of collateral clause. And you are going to hopefully have the seller agree beforehand that he will agree to accept the substitution of collateral or move his mortgage to

another piece of property that you shall designate in the future. He will cooperate if you are willing to prove to him that the moving of this mortgage from one property to the next does in no way jeopardize his position and guarantees in fact to enhance his position by giving him one of the sweeteners that we previously discussed.

2. Using This Technique to Raise Down Payments

Let's take a hypothetical example so that you can see how this technique might help you to raise the down payments for future investments. Suppose we're able to locate a $50,000 house with a seller carrying back a $15,000 second mortgage on the house itself, all with the understanding that in the future if necessary the seller will agree to a substitution of collateral as long as you will increase his interest rate, say, from 9¼ to 10¼ percent interest. Well, suppose time goes by and our $50,000 house now increases in value to $65,000. We have made monthly payments current to the seller on the $15,000 note that we owe him, and we locate a brand new investment which is selling for an excellent price that requires a $15,000 down payment. Suppose that the property we locate is a $100,000 building with an $85,000 contract of sale underlying mortgage, and it's worth maybe $110,000, but the seller needs $15,000 in cash and needs it quickly. How can I obtain my $15,000 down payment if I don't have any resources but the property that I purchased a year and a half ago? Will it be necessary for me to sell my first investment property in order to take advantage of this new investment? Well, if you've caught the vision of how to use the moving of your mortgage technique, we've convinced the holder of the second mortgage on our first investment property that he should be wise and move the mortgage from our first home to the $100,000 building. By moving this mortgage we increase his interest rate and perhaps even increase his security for his collateral. When the mortgage is in the process of being moved, we know that we will be refinancing our first investment property. And there will be an existing $35,000 loan against it with a $65,000 value. At that point we either can refinance the piece of property and pull out as much equity as we possibly can (perhaps $15,000 in cash), or we can borrow against the equities in the form of a second mortgage or a home equity loan. That provides the cash for going into our next investment, which is our $100,000 building. The moving the mortgage technique allows us to pyramid our existing equities into higher and larger pieces of properties without having to sell them.

With respect to this moving the mortgage payment, I remember one of our Eastern graduates who came to the class having just recently purchased five small $22,000 duplexes in a depressed area of his town. The seller took as a down payment $2,000 on each of the five units and carried back a second mortgage for the difference. There were, as I remember, on each of the units a $5,000 existing first mortgage, and therefore the seller had $15,000 worth of second mortgages on each of the five units. Can you see how much created equity our graduate was able to arrange once he understood the moving of the mortgage technique?

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◀ *Technique 37:* Creative Use of Mortgage Paper

This next technique depends on a very innovative application of mortgage paper. In this case the mortgage (trust deed) paper applies to a property other than the one you are buying, but it opens up the door for you to acquire the target property. I sometimes call this technique "Buy High/Sell Low." Here's how it works.

I have always said that one of the ways to be successful in anything is to do the exact opposite of what the world is doing. So let's take the tried and true formula Buy Low/Sell High and reverse it. Let's Buy High and Sell Low. If you were to do this with any other investment, you would lose your shirt. But real estate is a different story. I am going to show you how to buy a

property for $100,000, sell it for $80,000, and still make a $10,000 profit. That's right—to sell a property for $20,000 less than its purchase price and still make $10,000. And it will be win/win, of course. Have I got your attention?

Let's start with a seller of a $100,000 property. I pick $100,000 for ease of illustration. For the same reason, this property will be free-and-clear. The seller is not a don't wanter but he is slightly flexible. He wants $20,000 down and is willing to carry the balance of $80,000 on a long-term, amortized loan. He realizes that in today's slow marketplace, he has to carry paper, or he may not be able to sell. He might even accept a $5,000 price reduction for a quick sale. He places his ad in the classified section of his local paper. He is actively seeking a person to give him $20,000 cash plus $80,000 paper in exchange for his house.

In the same marketplace, advertising in the same classified section (although on a different page) are dozens of individual sellers of paper. For example, you might find in the Mortgages or Trust Deeds for Sale section of your paper a person who owns an $80,000 mortgage that looks fairly similar to the one that the above house seller is willing to accept. This mortgage holder sold his property several years ago, carried back a mortgage, and has been receiving monthly payments regularly ever since. The property which is the collateral for the loan has increased significantly in value, thus enhancing the security of the loan. The seller, for whatever reason, wants to sell this mortgage for cash. Because of market forces, he will probably part with his paper and be happy to receive 60 percent of its face value or $48,000 cash. Sometimes less.

Interesting. One person is looking for paper. And another person is willing to sell it—at a discount. Is there a way that we could get these two people together and profit from it in a win/win way without investing any of our own money? The answer is "yes."

Let's go to the seller of the paper and obtain a 45-day option to buy the paper for $48,000. You explain that you will need some time to arrange your financing. You try to tie up the right to buy the paper at a discount so that you will have time to put all of the pieces together.

Then you go to the house seller and make him an offer. You offer to give $20,000 cash down plus an $80,000 mortgage secured by another piece of property. The seller has already agreed to accept paper against his own property. The crucial link in this whole process is to get him to accept an existing piece of paper secured by another property (the paper that you can buy at a discount) instead of a new piece of paper secured by his own house.

How do you get a seller to accept a substitution of collateral? You show him the benefits—and there are many. First of all, the existing $80,000 paper has a proven track record. You can show the seller a history of regular monthly payments being made over a several-year period of time. That is much better than your promise to make payments on a new mortgage. The paper is "seasoned," as they say in the business. Secondly, the collateral will probably be better on the existing loan than on a new mortgage. In other words, the seller will be more secure with an existing loan on a more valuable property with a proven track record than with a new loan on his own home. Not everyone will accept this substitution of collateral, but enough people are willing to make it well worth the time and hassle to find them.

The next step is to get a loan against the $100,000 house. Since the property is free-and-clear and since the seller has agreed to accept an $80,000 loan secured by another property, that gives us a marvelous borrowing opportunity. Let's put an $80,000 loan against the seller's house. The $80,000 loan proceeds will be dispersed as follows:

> $48,000 to the seller of the discounted mortgage. He collects his money and walks away happy. Win/win.

$20,000 to the seller of the house. He collects his $20,000 cash plus an $80,000 mortgage secured on a property other than his own. He gets what he wanted without any dickering in price. Win/win.

$2,000 cash for closing costs to obtain the new loan. The bank makes a new loan, makes some fees, and has adequate security for the new loan. Win/win.

That leaves us with dispersals of $70,000 from the $80,000 loan proceeds. Where does the remaining $10,000 go? If you like, you can send it to me—but I expect that you'll just pocket it yourself.

Let's review, then: The house seller got what he wanted. The paper seller got what he wanted. The banker got what he wanted. And you ended up with $10,000 in cash plus a $20,000 profit in an investment home. With nothing out of your pocket—and of course, no balloon payments. Not bad for a month's work. Most Americans don't do as well in a year's time.

But suppose you don't like the thought of renting out this home, managing tenants, and paying the negative cash flow that will obviously be a part of this new, high-interest-rate first mortgage you had to obtain. Well, let's complete the circle in a win/win way. Do you suppose that at this very moment in your city there are people who still buy real estate the old-fashioned way: putting up a large down payment and refinancing at high interest rates? Although this seems ridiculous to us, knowing what we know, there are still hundreds of conventional buyers in the marketplace. In fact, I'll wager that there are dozens of buyers at this very moment who are buying $100,000 houses in your city, who are using their hard-earned $20,000 cash down payments and are agreeing to obtain high-interest first mortgages. They don't like it, but they don't know of any other way. Let's give them an alternative. Let's advertise our newly-acquired property in the following manner:

Nothing Down and
Guaranteed $20,000 Below the Market.

Do you think that headline might attract a few buyers? The conventional buyer who was willing to put $10,000 down and buy at market price can now keep his $20,000 cash and buy a property $20,000 below market. He buys your property with nothing down simply by assuming your mortgage. In one swift move, he has increased his net worth by $20,000 and still has his cash left to buy something else with. Probably something that goes down in value like furniture. Do you think that this is win/win to him? Of course it is.

So the end result is we buy a property for $100,000 and sell it for $80,000, pocket $10,000 cash, and everybody wins. This is not an overfinanced scheme with pyramids of unstable debt. This is conservative for everyone.

Now you might say that this is an awful lot of work just to make $10,000 cash. But if you had a system of doing this once a month . . . it might be worth the effort. I know a lot of people who make a third this amount and work twice as hard to get it. Give it a try. And incidentally, the idea for this technique is based on the work of Joe Land.

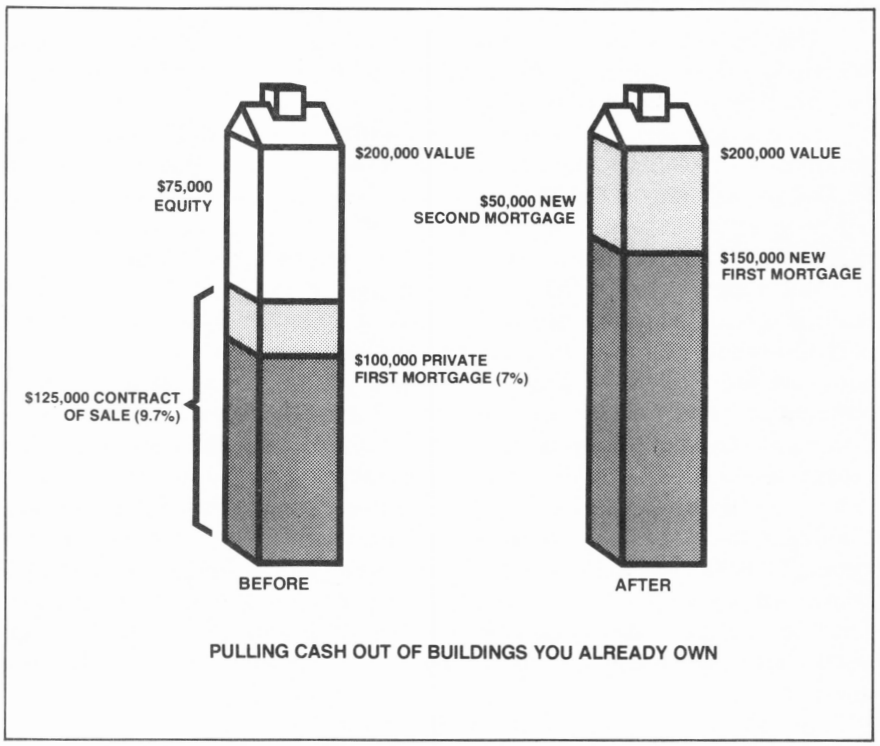
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[1]In earlier editions of this manual, Technique 37 was assigned to "Creative Refinancing of Underlying Mortgage," which dealt with "blended" financing. "Blended" financing refers to a situation where a lending institution permits a buyer to come in and refinance a low-interest mortgage at a rate that is somewhere between the existing rate of the note and the market rate at the time. This "blended" rate is win/win in that it permits the bank to relieve its portfolio of the low-interest note and permits the buyer to get in for less than the market rate. "Creative refinances" of this type (such as used by the Federal National Mortgage Association [Fannie Mae] in the United States) is particularly useful during times of very high interest rates. Frequently lending institutions will cater to this solution in order to move "R.E.O.s" (Real Estate Owner properties they have taken back through foreclosure) out of their portfolio. See the book *How to Write a Nothing Down Offer* by Richard J. Allen (pp. 206–207, 226–230) for more details.

Technique 38: ▶
Pulling Cash Out of Buildings You Own but Don't Want to Sell

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Now one other technique that also involves the flexibility of properties that are mortgaged by private lenders is the technique I call how to pull cash out of buildings you own but don't want to sell. I'm thinking of an example of property I purchased which is worth $200,000 to $250,000 at this time. The set-up is depicted in the diagram.



PULLING CASH OUT OF BUILDINGS YOU ALREADY OWN

There is an underlying first mortgage loan of $100,000 that is held by a private individual who receives monthly payments at 7 percent interest and has long since realized that it was a very foolish mistake to sell this property with such a low interest rate and such a long-term loan. We discussed the possibility of perhaps my refinancing the property that I own to raise cash for my future investment properties. The only problem that exists here is that if I refinance my $200,000 building, I could probably only get a new loan of about 75 percent, which is $150,000. If I pay off $135,000 of the underlying loan, I only have a $25,000 amount of cash left, less closing costs. The cost of refinancing is what makes it prohibitive. And in addition to that, I have a 9.7 percent mortgage rate which I would lose in the refinance.

In order to make the refinance more beneficial to us, we ask the underlying mortgage holder to share some of the loan proceeds. What we're saying here is that when the holders of the underlying first mortgage receive their check for $100,000 in cash for the refinance, they agree to lend us back $50,000 of it. We carry a $50,000 second mortgage on top of the brand new first $150,000 loan. They are in no position to complain because they get $50,000 in cash to reinvest at higher interest rates as well as receiving a higher interest rate on the new second mortgage. We better our position because we get to borrow our entire equity in the property without having to sell the property.

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Technique 39: ▶
Making a Partner of the Holder of an Underlying Mortgage

The last technique on dealing with people with underlying mortgages is to make a partner out of the holder of the underlying mortgage. Let's consider an example. Suppose we located a $50,000 building that has an existing $25,000 first mortgage and a $15,000 second mortgage which is held by a

private party. You find yourself in a situation where you do not have a strong financial statement nor do you have the $10,000 in cash that is necessary to buy this property. But you locate it, and you understand that the value is there and know that you could possibly buy the property with little or nothing down if you could convince the holder of the second mortgage to become a partner with you. Let's see how you could do that. How could you buy this property with little or nothing down using the holder of the second mortgage as the partner? Give me some solutions.

My Solution

The first solution is to have him lend you $10,000 in cash, which is probably quite unlikely. The second solution is to have him release his $15,000 mortgage and move it to another piece of property to give you the opportunity to borrow the necessary $10,000 down payment. But suppose you're not very strong. Maybe you could go to the holder of the second mortgage and say, "How would you like to be able to buy a half interest in your property back? I'm here to show you a way that you and I can own this building again; you'll get half interest, I'll get half interest, and we'll be able to buy this property from the seller." He says, "Well, I don't have $10,000 in cash." But what does he have? He has the ability to release his $15,000 second mortgage against the property, let you go down to the bank and borrow $10,000 on a second mortgage loan, give the $10,000 in cash to the previous owner, and have the holder of the second mortgage place a third mortgage of $15,000 on the property. This will give him a little bit less security, but it gives him half-interest in his property back again, and that's like increasing the interest rate for him.

There are all kinds of possibilities. Every time you talk with this holder of the second mortgage who is a private person you might be able to convince him to participate with you in the ownership of that property for certain kinds of benefits. This concludes our discussion of flexibilities with respect to holders of underlying mortgages, and we're now going on to the next section, which has to do with investors.

H. INVESTORS

Technique 40: ▶
Selling of Second Trust (or Mortgage) Notes

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I became aware of this technique when a graduate student of mine told me about one of his creative transactions. He told me that he had located a $28,000 piece of property, a small home in a very modest neighborhood. The sale price was $24,000. The owners were undervaluing their property in order to be able to sell it quickly for cash. There was an existing $16,000 loan against their property, and the sellers wished the $8,000 of their equity to be paid out in cash. Our student examined the details of the transaction, and the broker made the suggestion that he would help my student sell a $12,000 second trust deed note against this piece of property to an investor friend he had for $8,000 in cash. Let's look at the circumstances here. We have a $16,000 loan and a $28,000 value. That is $12,000 equity. But the broker was suggesting to my student that he create a $12,000 note at a going rate of interest with monthly payments for a certain period of time and then sell that to an investor for $8,000 cash. Let's examine the yield on an investment like this. If I have a note that is paying me $100 a month with a face value of $12,000, I receive $1,200 a year in the payment of principal and interest. Suppose it's just an interest only loan. If I am able to purchase that loan for a cash payment of $8,000, I'm still receiving $1,200 a year in interest, but I've only invested $8,000 into it. Although the note that I purchased bears an interest only rate of 10 percent, I only invest $8,000 cash, so my yield on my investment is $1,200 divided by $8,000 or 15 percent per year. That's a fairly substantial rate of return for an investor.

Now why would I as a purchaser of real estate investments be willing to create a $12,000 note that I had to repay in order to get $8,000 in cash? If I could create this note before I bought this property and sell the note and use the cash to buy the property with, then I would have a nothing down transaction. I may be paying $4,000 more for this property without any investment of cash on my own. The important things to understand here are that we are advertising in the newspapers for investors to come in, and we can offer them a yield of up to 15 to 20 percent return on their invested dollars, which is a substantial return. They are very thrilled about that return, and yet the seller gets his cash, and he's thrilled, and I get my property, and I'm thrilled. All three people benefit from this kind of a transaction. All it takes is for me to find someone who is willing to lend me that kind of money and secure this loan against the property that I want to buy. The investor is going to be very careful about lending money in this way. He is going to want to make sure that my collateral is adequate, that my credit rating is adequate, that the yield on his investment is adequate, and if all three of these things fall in line—the quality of the paper, the quality of the investor, and the quality of the collateral—then he should not be too worried about making that kind of an investment.

Another approach using notes creatively is as follows: Suppose I go into the marketplace and buy notes at a discounted face value. I might buy a $12,000 note for $8,000 in cash, knowing that I might be able to make money from that particular note. Suppose I go into the marketplace and locate a particular seller who is willing to accept paper for a portion of his down payment and is not concerned about what the security is for that paper. I might find someone who would accept my second mortgage note as a portion of the down payment on his property by accepting my note at full face value. Now if I know that I can go out in the marketplace and buy notes at the value of 75 cents on the dollar and can trade that as down payments on real estate at 100 cents on the dollar, then I'm gaining up to 25 cents on the dollar the second I buy a piece of property. Although that means I have to use cash to do this, I can significantly reduce the price of the property that I am buying and make a profit on the way in.

I. PARTNERS ("IF I DON'T HAVE IT, SOMEONE ELSE DOES")

Up to this particular point we have spent a great amount of time talking about how you as the beginning investor can learn how to find properties, learn how to negotiate with sellers, and learn how to use nothing down techniques to buy property. We have assumed up to this point that you have the adequate credit rating, the adequate financial strength, the adequate equity and properties that you own now, and the adequate strong job capability to carry yourself and to do your own investing. But suppose that you neither have property nor equity nor cash flow to support yourself, and you would like to begin to learn how to invest in real estate using nothing down techniques. This is where partnerships come in.

1. What Is a Partnership?

Now, when I use the word "Partnership" I don't want to scare you by using a complicated word that has a lot of negative connotations. A partnership is simply a joint venture between you and another creative person. He needs you, and you need him. He may have the strength that you do not have, but you have strengths that he does not have. It's a partnership of greed and need. You need him to make money, and he needs you to make money. You do a lot of the work; he adds certain benefits.

2. An Illustration

The first real partnership I ever entered into was in the location of an approximately four-acre piece of ground zoned for apartment construction. It was owned by The Church of Jesus Christ of Latter-day Saints and had been given to them as tithing many years previously, and as this property had been held by the Church, the city had grown up around it, and there were very large apartment complexes adjacent to it. It was a beautiful prime piece of property. I learned that the Church was interested in selling this piece of property and approached one of the agents who worked for the Church and got some information about the property itself. He told me that he had received several offers to purchase the property, but they did not feel that the offers were adequate. They had one offer for $150,000 in cash and another offer for a little bit less than that, but they felt that the property was worth well over $200,000. I checked with a real estate appraiser, and he gave me the opinion that the property would be worth approximately $2,500 per unit of buildable apartment ground. I checked with the city and found out that 80 units could be built on this particular piece of property, and therefore, since they could build 80 units, it would be worth approximately $200,000 to an investor. The agent for the Church indicated to me that he would be willing to sell me an option on this piece of property for $5,000 with the right to purchase that property in one year for $200,000. This was a very large figure to me and almost boggled my mind, being a young investor, but I felt that there was some potential profit there so I began to pursue it.

My first problem was that I didn't have $5,000, and the second problem was I wasn't really sure if the property was worth $200,000 or not; and if it was worth $200,000, what should I do to verify this and to sell the property to a higher bidder. I decided to proceed and went back up to talk with the agent and expressed to him that I did not have $5,000, and he said, "Well, then, I'll let you purchase the property with a $2,500 option amount now; we'll lock the price in a for year at $200,000. If you can't come up with the $200,000 in cash at that time, we'll let you pay equal installments of $50,000 plus interest each six months thereafter until the whole lump sum is paid in full with appropriate lot releases if necessary." I agreed to those terms and left his office with one very large problem on my mind. I didn't even have the $2,500 and needed to know how to get it.

As I was sitting in a dentist's chair a few days later, the solution came to me. "If I don't have the money, perhaps I can convince someone else who has the money to come in with me as a partner." The dentist put up the money and became my partner when I explained the benefits to him. This I did not learn out of a book; I did not learn it from some fancy real estate course. Although these ideas are very prevalent, they came out of my need to make a profit. And I found when a person locates a good investment to purchase and doesn't have the money to buy it and can see a very substantial profit going down the drain if he doesn't act, then there is sufficient impetus for him to overcome the shyness and the fear that he has of talking to other people about entering into a partnership with him to make a profit. We structured the transaction so that the $2,500 was given, and nine months later, to make a long story short, we sold that same piece of property to a builder who was looking for that type of land for the price of $280,000 less commissions and costs. Now in that transaction over $70,000 profit was generated for me, my dentist friend, and my real estate broker.

3. "Half a Piece of Pie Is Better than No Pie at All"

That was the first real experience I had in making money with other people's money. And I began to realize that if I didn't have the money, I surely could learn how to borrow it from other people, or I could use their financial strength to borrow the down payments necessary for other investments if the opportunities arose. Then I began to pursue this particular course. I realized that if I could make money with other people's money, that I would never have any trouble finding other investors because the word would spread. My motto is that a half of a pie is better than no pie at all. But sometimes it takes an investor or two at the very beginning of an investor's career to get him enough profit with his partners to start out on his own. Sometimes it takes just a little bit of shove or assistance from a partner to get our own individual snowball rolling down the hill. Then once the snowball starts, it's self-generating.

4. Finding Partners

How do you find a partner? You have friends and relatives and business associates, even the seller himself as we mentioned in other particular examples of techniques. There are opportunities in advertisements such as the one that we have included below:

> Earn 10-12% on your money secured by prime real estate.
> Profit can go higher. Call Bob, 802-838-4777.

You should not be afraid of approaching someone and asking them for money, especially if you have an excellent investment to show them. You could approach them and say, "I have located a beautiful piece of property at such and such an address and such and such a location, and I need another $5,000 to $10,000 to put it together. Are you interested in making money?" Now most people have their money invested in a savings account or the stock market or other assets that appreciate at 6 to 10 to 12 percent a year. If you could show them how to make 30 or 40 and sometimes 50 percent on their money each and every year, you could easily convince them to lend you this money to enter a partnership with you. However, check with competent legal advisors to make sure your procedures don't violate any regulations. Stay above-board.

5. Convincing a Partner that He Should Lend You His Money

Let's look at how you can convince a partner that he should lend you money.

a. Compare Bank Rates. Six percent secured savings accounts versus 12 percent trust deeds (or mortgages). Appeal to his greed without sounding flaky. A blanket mortgage usually works here. He feels secure that you are

going to put yourself into the partnership because you are willing to risk some of your own equity.

b. Offer Security. A second trust deed (or mortgage) against your own home. The property will be in his name with a side partnership agreement between you. Don't be too generous. Give only what is necessary.

c. Offer Expertise. Convince him that you know what you are doing. Perhaps you can show him pictures of properties you have purchased and made money on. Give him the names of other satisfied partners.

d. Offer Time. A busy person sometimes will consider partnerships because he does not have the time to do the looking. Professional people are vulnerable to this argument. Real estate agents can use this perfectly.

6. Rules to Follow in Setting Up Partnerships

a. Don't Use Them Unless You Have to. One of the rules in setting up a partnership is: don't use it unless you have to; it is very expensive. Many of us worry about paying up to 18 percent interest on our bank loans. We cringe at that. But do we realize that if we bring in a partner and he takes half the profit, we are paying as high as 50 percent of the total profit, and that's very expensive money. Don't use them unless you run out of your own money and can't proceed on your own.

b. Define the Contribution of Each in Writing. Define the contribution of each partner, e.g., your money, my time. Put this in writing. You will supply the down payment for the investment and any other additional funds that may be necessary to keep this investment alive. You will provide half the negative cash flows, and I will provide half the negative cash flows as your partner. I will handle the management of the property, and I will make sure that all the details are taken care of. Make sure that all these kinds of things are written out so there is no misunderstanding down the road. Have a competent attorney draw up a partnership agreement for you.

c. Maintain Maximum Control. Maintain maximum control means that as much as possible you should maintain the upper hand. You are the expert; you are the person who is going to dictate whether or not you should sell. In the very beginning you may find that it is very difficult to maintain a control like this; you might, as a matter of fact, have to put the property in the name of your partner so that he can feel very protected so that he knows that the property must make money, or he will not share any profits with you. However, as you gain more expertise and more confidence as you go down the road with other investments with the same partner, you can convince him that it would be better for him to listen to your advice rather than maintaining control himself.

d. Keep Each Relationship on a Per-Property Basis. Partnerships are very difficult to get out of. Don't get into a marriage on a long-term basis with only one partner because it limits your flexibility. Explain to him that you will buy this one property together. If things work out, you will continue. "If things don't work out, you are free to go your way, and I am free to go mine. At any time during the partnership relationship, if I find an investment that I like that I can handle by myself, I will buy it by myself. If I want to go in with another partner for another investment, I will do so. You and I are only in on this property on Elm Street."

e. Avoid Short-Term Payoffs. Avoiding short-term payoffs to partners is a very important rule because if we have to spend our time constantly looking for money to repay our short-term loans to our partners, we take away the creative power that we need to use to locate other investment property and to continue our investment and accumulation program. I don't want to have to take time out from my precious investing program to go find another partner to borrow from just to pay off an existing loan. I want to be able to use up my creative time to look for more pieces of property. Try to explain to your partner that this will be a long-term investment, that your funds will not come along until the property is sold. The property may not be sold for several years. This is a "patience" investment.

f. Establish a Buy-Out Clause and a Division of Profits Agreement. This means that if you are ever dissatisfied with this agreement, you can buy me out or if you wish, I will buy you out. We will go down and have two or three separate individual appraisals done on each property that we own together; we will take an average of the three; then flip a coin, and whoever wins can buy the other person out. If he doesn't have the money to buy the other person out, then he would have to sell. Make it simple and straightforward. Although you may not want to sell the piece of property, it would be better for you to take your profit and get out and go on your own avenues than to be stuck with a disgruntled partner.

g. Draw Up an Agreement. Finally, you would be wise to visit with an attorney to draw up a simple partnership document. Agreements can be as formal or informal as you deem necessary. I have gone from no written agreement to a $300 document drawn up by an attorney. The most simple procedure is to have both of your names on the deed so that neither partner can sell without the permission of the other partner. Establish undivided one-half interest as tenants in common. This insulates you in event of bankruptcy of either partner. Check with professionals on the details.

Example

I, _____, hereby agree

to borrow from _____, the sum of

$ _____. The security for this sum is a trust deed on

a property located at _____.

Special terms:

Signed _____

Date _____

7. A Challenge

The goal that we need to set for you is a challenge to find at least one person with $25,000 that you can borrow if you need it at any time you want, as long as he can be secured by the property you are buying and while protected in his investment. Now if you don't want to find one person with $25,000, I might challenge you to find five people with $5,000 a piece. This should not be difficult. There are many chicken-hearted people out there who know that they want to invest in real estate but don't have the courage or the time or the

expertise to do so. You are their saviors. You are helping them make more money. You are helping them become financially independent. They are carrying you on their backs towards their financial independence and by making money for them, you make financial independence for yourself. It's a way for you to develop an initial nest egg for you to get started. That is once again a challenge: one person with $25,000 or five people with $5,000 apiece. It's important. It's necessary. Don't overlook this particular part of the program. Someday you may be extremely upset for not having followed this counsel.

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8. Five Creative Techniques for Using Partners

◀ *Technique 41:*
Borrowed Financial Statement

The partner provides financial strength by loaning you his financial statement. His name is placed on the mortgage with yours, but he gives you a quitclaim deed for his interest in the property. You give him cash for his efforts or a note to be paid off in the future. He signs on the mortgage, and you cosign. It is as if he is buying the property, and you are just an afterthought. However, once your name is associated with a mortgage, this gives you more strength in the future. As soon as you can, you will go in and put the mortgage in your own name and remove his. In the case of a default by you, if you can't make the mortgage payments for a period of three months, you can give him the option to come in and make the delinquent payments to protect his credit rating. Of course, you would have to relinquish your equity to him.

◀ *Technique 42:*
Borrowed Money for Down Payments

You could borrow, say, $10,000 from a person with considerable savings, using an interest percentage of perhaps 15 percent. Be careful on guaranteed profits; you might trigger the application of Securities laws and regulations. Secure your borrowings by a second trust deed (or mortgage) on the property you are going to buy. You can give the partner a percentage of the action if he needs it. Make sure you don't violate usury laws in your state or province.

◀ *Technique 43:*
Borrowed Down Payments until Your Money Comes

You buy the property, and I will pay you back as soon as my money comes from another source. We split the profits. In addition, I pay you at least a 10 percent profit on the money I borrow from you.

◀ *Technique 44:*
Your Cash Flow/My Equity or Some Combination

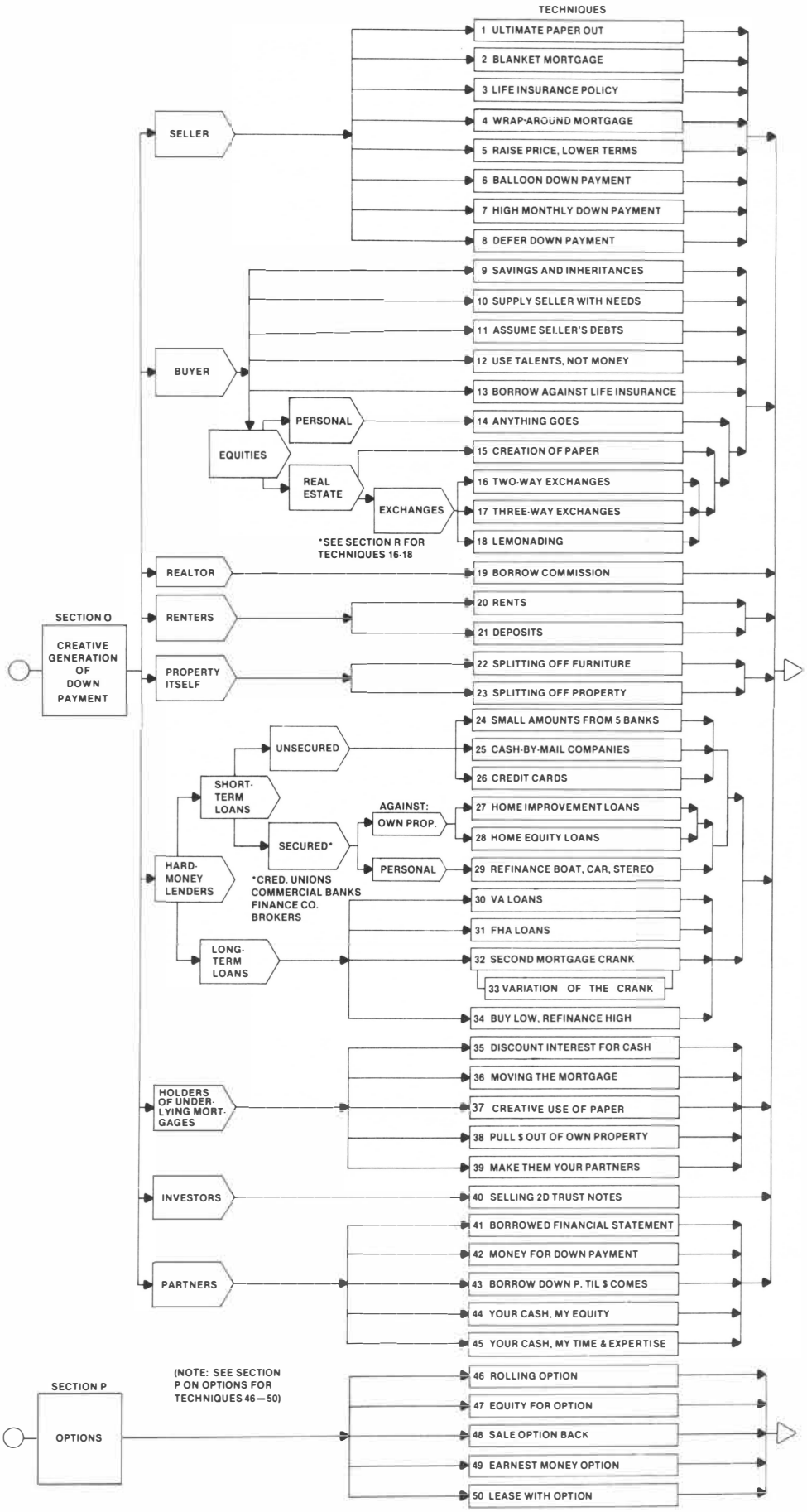
Your partner may have a high monthly cash flow but no cash for down payments in a lump sum. He may also have large amounts of equity but no knowledge of how to use them to make money. You could use your expertise for a split of the profits, or you may wish to contribute your equity, cash, or cash flow to a partnership. This technique lends itself well, also, to tenant-equity participation arrangements already discussed in Section K, item C.

◀ *Technique 45:*
You Put Up the Cash; I Put Up the Time and Expertise— We Split 50/50 Percent

This is an excellent way for a partner to double or triple his yield on money in a savings account, and it's an excellent way for you to start out if you don't have any cash. It's a beautiful partnership motivated by greed and need.

Note:

The chart that appears on the next page will provide an overview of all the techniques that we have discussed to this point. (See Section R on Exchanges for Techniques 16 through 18. See Section P on Options for Techniques 46 through 50.)


TECHNIQUES
1 ULTIMATE PAPER OUT
2 BLANKET MORTGAGE
3 LIFE INSURANCE POLICY
4 WRAP-AROUND MORTGAGE
5 RAISE PRICE, LOWER TERMS
6 BALLOON DOWN PAYMENT
7 HIGH MONTHLY DOWN PAYMENT
8 DEFER DOWN PAYMENT
SELLER
9 SAVINGS AND INHERITANCES
10 SUPPLY SELLER WITH NEEDS
11 ASSUME SELLER'S DEBTS
12 USE TALENTS, NOT MONEY
13 BORROW AGAINST LIFE INSURANCE
BUYER
PERSONAL
14 ANYTHING GOES
EQUITIES
15 CREATION OF PAPER
REAL ESTATE
16 TWO-WAY EXCHANGES
EXCHANGES
17 THREE-WAY EXCHANGES
18 LEMONADING
*SEE SECTION R FOR TECHNIQUES 16-18
REALTOR
19 BORROW COMMISSION
SECTION O
CREATIVE GENERATION OF DOWN PAYMENT
RENTERS
20 RENTS
21 DEPOSITS
PROPERTY ITSELF
22 SPLITTING OFF FURNITURE
23 SPLITTING OFF PROPERTY
UNSECURED
24 SMALL AMOUNTS FROM 5 BANKS
25 CASH-BY-MAIL COMPANIES
26 CREDIT CARDS
SHORT-TERM LOANS
AGAINST:
OWN PROP.
27 HOME IMPROVEMENT LOANS
28 HOME EQUITY LOANS
SECURED*
PERSONAL
29 REFINANCE BOAT, CAR, STEREO
HARD-MONEY LENDERS
*CRED. UNIONS
COMMERCIAL BANKS
FINANCE CO.
BROKERS
30 VA LOANS
31 FHA LOANS
LONG-TERM LOANS
32 SECOND MORTGAGE CRANK
33 VARIATION OF THE CRANK
34 BUY LOW, REFINANCE HIGH
35 DISCOUNT INTEREST FOR CASH
36 MOVING THE MORTGAGE
HOLDERS OF UNDER-LYING MORT-GAGES
37 CREATIVE USE OF PAPER
38 PULL $ OUT OF OWN PROPERTY
39 MAKE THEM YOUR PARTNERS
INVESTORS
40 SELLING 2D TRUST NOTES
41 BORROWED FINANCIAL STATEMENT
42 MONEY FOR DOWN PAYMENT
PARTNERS
43 BORROW DOWN P. TIL $ COMES
44 YOUR CASH, MY EQUITY
45 YOUR CASH, MY TIME & EXPERTISE
SECTION P
OPTIONS
(NOTE: SEE SECTION P ON OPTIONS FOR TECHNIQUES 46—50)
46 ROLLING OPTION
47 EQUITY FOR OPTION
48 SALE OPTION BACK
49 EARNEST MONEY OPTION
50 LEASE WITH OPTION

Creating Wealth

WITH LITTLE OR NOTHING DOWN

Manual

The Nothing Down System of Creative Financing in Real Estate Investments

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SECTION P

Options

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Options

P

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Options

P

And now we come to the final form of nothing down transactions, and that is the use of options. The world of using options is extremely powerful because an option is the ultimate form of leverage. It is the use of the smallest amount of down payment with the greatest amount of potential profit.

A. WHAT IS AN OPTION?

An option is the privilege or the right to be able to purchase a piece of property at a future date at a fixed price which is determined now. If I locate a 16-unit apartment building which is selling now for $400,000 and I give the seller a $2,000 cash payment to purchase an option to buy his property 18 months from now for a price of $500,000, then I am paying my $2,000 for the privilege of being able to lock his price in for an 18-month period of time.

1. Benefits and Detriments

What are the benefits and the detriments of an option? Why in the world would the holder of that 16-unit apartment building even consider giving me an option to buy his building in 18 months for a $500,000 price? Obviously, if he were to be able to receive $2,000 cash now, that would be a benefit that he could spend tax-free without even having to report it as taxable income until the option was exercised 18 months down the road. And if he were to accept an option of this kind, he obviously must disagree with me that the price of the property will have risen to a $500,000 figure by that time. He obviously is betting against me. He thinks that I am going to be wrong, that his property will not be worth $500,000 by that time. Therefore, to accept the $2,000 now would be just free money because the property is not going to be worth as much as I think it will be. As the investor, on the other hand, I believe that the $2,000 is very well spent because the price of the property is probably going to be more than $500,000 according to my educated estimates. And therefore I am giving him a small amount of cash now for the privilege of making a large profit in the future. He is betting against my opinion, and I am betting against his opinion. Whoever wins the bet makes the money. If the property is not worth the $500,000 in 18 months, he keeps my $2,000 as an option and is $2,000 to the better; I am $2,000 to the poorer. If, however, the price of the property has increased above $500,000, then I make the increased profit by exercising my option. Market knowledge is therefore very important when investing in options.

An option has the benefit to a purchaser that the title to the profit remains in the name of the seller until the property is ultimately purchased, and the option is exercised. This eliminates the problem of having to do management and having to pay taxes and negative cash flows, etc. As far as the seller is concerned, he will also benefit because he gets to keep the property and maintain his tax shelter until the property is ultimately purchased.

2. "A Tale of Two Cities"—A Million-Dollar Example of an Option

A broker in our area located a very beautiful 40-acre tract of ground. It was located between two growing cities. The farmer had deliberately maintained his ground outside the city limits of both of the growing cities because he did not want to have to pay high city taxes. His ground was worth approximately $20,000 to $25,000 an acre in subdivision value, and he probably could sell his 40 acres of ground for $25,000 an acre and make his million dollars' profit and retire. A very astute broker in our area knew that one of the cities was losing tax base to the other city, which was growing faster. And he approached the mayor and the councilmen of the city and made arrangements with them to rezone this 40-acre parcel of ground to commercial property and to annex it into that city in order for them to increase their tax base. Then he went to the farmer and gave him a $10,000 cashier's check if the seller would give him an option to be able to buy that ground in six months for a million dollars in cash—no terms, just solid cash. The farmer thought to himself, "Well, there are two things that can happen. Either he is going to be able to pay me a million dollars in cash, which is fine—it's the sale I'm looking for, and I'll be a million dollars richer—or he won't be able to perform on the option, and I will receive a $10,000 cashier's check. Either way I win." So he accepted the check and signed the option.

Then the broker proceeded immediately to locate a major mall company that was looking for space between the two cities and negotiated to sell this land to them at commercial rates. Instead of selling for $25,000 an acre, a 40-acre tract of commercial ground might be worth two or three dollars a square foot, which might be anywhere from $80,000 to $125,000 an acre. The man negotiated to sell this ground very cheaply at $50,000 an acre. The mall company purchased the land for $50,000 an acre, and in the escrow the broker received for his $10,000 risk a million-dollar check.

Now you only need to do that kind of transaction once! And that's why I'd like to have you keep your eyes open. That's why it's important to have you visit with the planning and zoning commission officials to learn what is going to happen in the future. Some owners don't understand how valuable their land is going to be because they don't understand the future plans for their communities. But if you are one step ahead of the general public knowledge, you can make money by optioning pieces of ground before they become extremely valuable.

3. Techniques

Let's look at some examples for some techniques for the use of options, which might become handy in the near future for those of you who want to get heavily involved in the investment world.

Technique 46: ▶ The Rolling Option

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One of the first uses of an option is to enable a developer to purchase large portions of ground. I'll give you an example. Sometime back, I was looking at a 100-acre parcel of ground in a growing area which the seller wanted to sell in one large package for development of housing tracts. He wanted $18,000 an acre, total price of $1,800,000. There were no loans against the property. $1,800,000 is a very large amount of money. And it would probably take from three to five years to be able to develop that 100 acres of ground in this particular community. This would mean that if I purchased that ground now, I'd either have to have $1,800,000 in cash to invest and to tie up for a five-year period of time, or I would have to pay interest on that land as I purchased it from the seller. And that is not palatable either; 10 percent interest on $1,800,000 is well over $180,000 a year in interest alone just to carry the land. I proposed to him that I pay him the cash and have him deliver five acres free-and-clear (5 acres × 18,000 = 90,000). Inherent in the purchase of the initial five acres was an option to be able to purchase 10-acre tracts thereafter each year for the next five years until the entire project

would either be developed or the options would be relinquished.

In other words, I would buy a tract of land with a $90,000 down payment. I could develop it, build houses on it, take my profit and buy another ten-acre tract of land. If I continued to have success, I could roll my option to the next parcel of ground and continue rolling that option from tract to tract to tract until the final 100-acre parcel was completely developed. I would not have to have high interest carrying costs, but the options that I would negotiate with the seller would be at higher and higher prices per acre until at the end of five years the seller would still make the same amount of money but would eliminate the necessity for me to have to carry that in monthly interest payments.

This is called the *rolling option.* I buy one piece of property with the option to buy another piece within a certain period of time and to roll that option to the next piece of ground until the entire parcel is finished. This approach is very common and predominant in the land development business.

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◀ *Technique 47:*
Equity for Options

Many people are under the mistaken impression that in order to obtain an option on a piece of property, they have to use cash. This is not so. Many of you have investment houses or boats, stereos, etc., and you can use anything you have as equity on a piece of property. I have often said that if a person has a recreation lot that they have never seen or never intend on using, it would be much better for them to locate an individual who has a piece of ground and who is willing to sell an option on his property and give him a recreational lot as the option fee. If you have a dead equity that you're not using, get rid of it. Use it as an option to increase your net worth somewhere down the road. You have to be careful; you need to know the value of property; you need to have some inside information. Still it can be very successfully worked out.

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◀ *Technique 48:*
Sale Option Back

Let's take an example of the fellow who has five acres worth of ground that is two, three, four years away from eventual development. It's now on the fringes of the city and is in a green belt area and cannot be developed for several years; he wants to be able to sell this land, but he knows that if he were able to sell his land, he'd have to take a substantial discount. He can't borrow against his land, and so he says, "Well, I guess I'm just locked into keeping this land for the future without being able to take funds out and reinvest them into income-producing property."

There is a way, however, to have your cake and eat it, too. Suppose this five-acre piece of ground is worth about $100,000 at $20,000 an acre, but you know that because of future plans, the city is anticipating that it might be in the commercial zone five years down the road, and it therefore may be worth as much as $200,000 or $300,000 or $400,000. If you sell your land now, you'll not be able to take advantage of that future growth, but if you don't sell your land now, you will not be able to invest your money into income property, which is something you'd like to do. How can you have your cake and eat it, too?

Take this $100,000 piece of property and advertise it on the market with substantial discount and sell it for $80,000 in cash with the option to buy it back in three or four years for a fixed price of $120,000. This way you are discounting the value of your property for $80,000, which you can now go out and invest. However, you know that if the value of the property does significantly increase some time in the future, you are able to buy that property back and take advantage of the increased profit. And the fellow who buys this land from you only has to wait his three- or four-year option period to see which way he wins. If the property is purchased back by exercising the option, then he has sold it for $120,000 and makes a 50 percent

profit on his money invested, which is a substantial return. If, however, the option is not exercised, then he makes the additional amount of profit that you would have normally made. That is the way to have your cake and eat it, too.

B. THE OPTION FORM

An Option form is included here to illustrate all of the usual kinds of necessary clauses.

1. Importance of the Extension Clause

The clause number 3, the extension of the option, is extremely important. You should always build into your options at least one extension or two extensions whereby you can pay an additional option fee and have the option extended for an additional period of time just in case you have not been conservative enough in your ability to raise the cash to buy this property. You don't want to leave yourself hanging high and dry.

C. MORE TECHNIQUES

There are two remaining techniques, the earnest money option and the lease with an option to purchase.

Technique 49: ▶ The Earnest Money Option

49

The earnest money option is probably one of the most powerful techniques that we are going to be able to talk about. It involves the use of very, very small amounts of cash and the ability to make quite a large amount of money. Once again, the most important bit of knowledge that we have to cultivate in becoming successful in using this option technique is our ability to analyze the marketplace and determine immediately what a property is worth with respect to other properties on the marketplace at the same time. Whenever you locate a piece of property that is selling for a price that is substantially below the market price, because of the seller's particular financial circumstances, you don't have to be scared away by the fact that you don't have a lot of money to invest in that piece of property. All you need really is enough money to make an "earnest money agreement" to purchase that property within a certain period of time.

1. What Is an Earnest Money Agreement?

An earnest money agreement (also known by a variety of other names depending on location, e.g. contract to purchase, agreement to purchase, offer to purchase, interim agreement, etc.) is nothing more or less than a very short-term option. It gives you a right to place a deposit of say $500 to hold the property's price locked in now, with the opportunity to buy that property within a six-week period or as long, say, as three months. If you fail to complete the purchase of that property within the prescribed period of time, you are liable to lose your earnest money or your deposit. The arrangement is therefore essentially much like an option. If you are able to complete your transaction, then your earnest money is applied towards the sales price.

2. An Example: Turning $500 into $9,000

Let's take an example of how this kind of option agreement works and note the kind of consideration that you go through to feel comfortable with it. A short time ago I located a beautiful 12-unit apartment building that was located in an excellent location but required a down payment of $50,000. This not only violated my standards of percent down payment, but it was also impossible for me to come up with that amount of money within the short period of time that the seller wanted it. He did have to have his $50,000 within a seven-week period of time. I did not have these funds available, and yet I did not want to see such an excellent piece of property bought by

"THIS IS A LEGALLY BINDING CONTRACT. IF NOT UNDERSTOOD, SEEK COMPETENT ADVICE."

OPTION

KNOW ALL MEN BY THESE PRESENTS:

That ..... of ....., hereinafter referred to as "Seller, hereby agrees for and in consideration of ..... ($.....) Dollars, paid by ..... of ....., hereinafter referred to as "Buyer", as follows:

1. PROPERTY: Seller hereby gives and grants to Buyer and to his heirs and assigns for a period of ..... months from the date hereof, hereinafter referred to as "First Option Period", the exclusive right and privilege of purchasing the following described real property located at ....., County of ....., State of ....., and more particularly described as follows:

Together with all water rights appurtenant thereto or used in connection therewith.
(Said real property and improvements, if any, shall hereinafter be referred to as "The Property").

2. PRICE. The total purchase price for said property is ..... ($.....) Dollars, payable in lawful money of the United States, strictly within the following times, to-wit. All sums paid for this option and any extension thereof as herein provided, shall be first applied on the purchase price, and the balance shall be paid as follows:

3. EXTENSION OF OPTION. Upon payment by Buyer to Seller of an additional sum of ..... ($.....) Dollars, cash or by cashier's check, prior to the expiration of the first option period, this option shall be extended for ..... months, hereinafter referred to as "Second Option Period". Upon Buyer's payment to Seller of a further sum of ..... $.....) Dollars, prior to the expiration of the second option period, this option shall be extended for a third period of ..... additional months, hereinafter referred to as "Third Option Period".

4. EXERCISE OF OPTION. This option shall be exercised by written notice to Seller on or before the expiration of the first option period, or if extended, the expiration of the second or third option periods as the case may be. Notice to exercise this option or to extend the option for a second or third option period, whether personally delivered or mailed to Seller at his address as indicated after Seller's signature hereto, by registered or certified mail, postage prepaid, and postmarked on or before such date of expiration, shall be timely and shall be deemed actual notice to Seller.

5. EVIDENCE OF TITLE.

(a) Promptly after the execution of this option, Seller shall deliver to Buyer for examination such abstracts of title, title policies, and other evidences of title as the Seller may have. In the event this option is not exercised by Buyer, all such evidences of title shall be immediately returned without expense to Seller.

(b) In the event this option is exercised as herein provided, Seller agrees to pay all abstracting expense or at Seller's option to furnish a policy of title insurance in the name of the Buyer.

(c) If an examination of the title should reveal defects in the title, Buyer shall notify Seller in writing thereof, and Seller agrees to forthwith take all reasonable action to clear the title. If the Seller does not clear title within a reasonable time, Buyer may do so at Seller's expense. Seller agrees to make final conveyance by Warranty Deed or ..... in the event of sale of other than real property. If either party fails to perform the provisions of this agreement, the party at fault agrees to pay all costs of enforcing this agreement, or any right arising out of the breach thereof, including a reasonable Attorney's fee.

6. CLOSING ADJUSTMENTS. All risk of loss and destruction of property and expenses of insurance shall be borne by Seller until date of possession. At time of closing of sale, property taxes, rents, insurance, interest and other expenses of property shall be prorated as of date of possession. All other taxes, including documentary taxes, and all assessments, mortgage liens and other liens, encumbrances or charges against the property of any nature, shall be paid by Seller except

.....

7. POSSESSION. Seller agrees to surrender possession of the property on or before ..... days following written notice of the exercising of this option by Buyer.

8. The Seller recognizes ..... Real Estate Company (Broker and Agent) through its salesman .....; as the Real Estate Broker with whom Seller listed this property for sale, and Seller agrees to pay a commission to said Broker equal to .....% of the gross sale price; and Seller hereby authorizes the agent to withhold such commission from the proceeds of sale at time of closing.

9. If this option be not exercised on or before the dates specified herein for exercise of same, the option shall expire of its own force and effect and the Seller may retain such option monies as have been paid to the Seller as full consideration for the granting of this option.

IN WITNESS WHEREOF, the Seller hereunto has set his name this ..... day of ....., 19.....

SIGNED IN PRESENCE OF:

.....

.....

.....

Seller

Address of Seller: .....

.....

someone else, and so I immediately analyzed the situation and noticed that the price was some $30,000 or $40,000 below the market at that time. I, therefore, gave the seller a check for $500 and purchased his property with the agreement that I would give him $50,000 in seven weeks, and if I didn't do that, I would lose my deposit. Thereafter I immediately began searching for someone who would be able to put $50,000 down as a down payment on this property to take advantage of the extreme under-market situation. I located a well-to-do individual who was looking for investment property. I negotiated with him to buy the property for $10,000 more than I had agreed to purchase it for. He gave me eventually $9,000 in cash for the right to assume my position and to buy the earnest money agreement from me so that he could go and close in my name and obtain the property. Therefore, the down payment he had to come up with was $59,000—$50,000 to the seller and $9,000 to me.

Why would he do such a thing when he knew that I was making an additional profit? He had his advisers go look at the property, and each one of them advised him that the price was excellent, that the terms were reasonable, and that he should not delay, that he should buy. I was able to make that $9,000 because I recognized an extremely profitable situation and took advantage of it, and then I found someone who could complete the transaction. I did not sell the property because I did not own the property. I only sold my "interest" in the property as set forth in the agreement that I held between myself and the seller, which stated that the price was locked in at a certain figure.

3. Safeguards to Observe

Now, there are several safeguards that need to be taken here for the investor who plans to use the earnest money option technique.

a. Know Your Marketplace and Act Quickly. First of all, know your marketplace. Next, remember that you don't "steal" in slow motion. If you find a property that is an excellent investment, buy it with the longest term closing in the future that you can negotiate.

One of the groups of investors in our area located a beautiful tract of ground that was being sold by a farmer. The farmer agreed to accept a $200 earnest money or deposit now, with a nine-month closing in the future. During this nine-month period of time, when the price of the property was locked in, they went down and had the land rezoned to condominium high-density units and were able to sell their interest in that property, in the paper really, the earnest money agreement, for a price of $125,000. They were cognizant of the value of the property. They increased it by rezoning, and they took advantage of their profit by selling it to a builder who could use the land in his building business.

b. Know Your Liability. The next thing you need to be careful about is your liability. You want to make sure that the deposit agreement states explicitly that your only liability in case of default on your part is your forfeiture of your deposit or (earnest money). In some areas, standard forms state clearly that the buyer shall forfeit up to 3 percent of the value of the property in case of default. This kind of clause should be struck out of the agreement. This adjustment is totally legal as long as the seller agrees to it. You should add a different clause that may say something like this: "In case of default, the buyer's only liability is to the extent of his deposit (earnest money). The forfeiture of his deposit (earnest money) is the only liability he shall incur."

c. Know Who the Willing Investors Are. You would not want the seller to come back and sue you for damages when you could not perform. To avoid that

probability, it is very wise to be able to establish relationships with other investors in your marketplace. Get to learn who does the buying and who has the money to invest. And try to understand their criteria so that if you ever run onto a piece of property that seems perfect for them, you can exercise an earnest money agreement and go "sell" that earnest money agreement to them. By having investors lined up this way, you don't have to worry about being out in the marketplace without anybody to sell your earnest money agreement to. Try to be able to have sources to close on a transaction if necessary in a short period of time and to turn around and to resell the property for a profit.

In California, for example, this technique is widely used for buyers of tract homes, and in some areas people camp out overnight for the privilege just to be able to buy a property. In some instances they turn around and sell their right to buy one of these homes for as much as $10,000 in cash.

d. Care in Taking Options in Condominium Developments. Other wise investors have gone into condominium development and purchased a condominium or two on the front end when the condominiums were just in the pre-development stages. An earnest money agreement locks the price in now without the possibility of closing on the transaction until the project is done, maybe seven, eight, ten months down the road, during which time the property may have considerably appreciated in value.

If I were going to go ahead and do this type of speculation—and it is speculation—I would be careful about the properties selected. If you want to buy a condominium unit, make sure it is a good unit and easily resellable, located perhaps in the best location, and on the right kind of floors, next to the golf course or whatever, easily resellable and easily showable.

e. The Right to Show the Property. The next thing you should watch out for is to put in your earnest money agreement a clause assuring you the right to show the property to prospective "tenants" or clients even while the seller may be living in this property. Suppose you located a home for $60,000 that the seller is willing to sell for $49,000. Go ahead and tie up the property for a two-month closing and then you have several months to find another buyer. You're going to have to be able to make the seller agree to let you show that person through the property.

f. Assuring the Right to "Assign" the Contract. Also, in your agreement to purchase, you should always place wherever your name is mentioned "John Doe and/or Assigns." This gives you the legal privilege to be able to assign this contract to another person if you so wish to do so, thereby making the agreement to purchase legal and viable as an instrument for carrying out this technique.

g. Weasel Clauses. You should also use several contingency clauses if necessary—subject to inspection by your partner or subject to the obtaining of financing—so that if you are not able to locate a new buyer, you can back out of the transaction gracefully. I am not recommending here that you lead people on by having them assume that their property has been sold when really in fact you are just trying to resell their property for a profit. You should sincerely try to close on the transaction as you said you would but by using your best efforts to locate a qualified buyer for it so that you don't actually have to go through with the transaction for yourself.

h. Also a Bit of Caution about Selling Your Option. "The greedy become the needy." Price your property below the market or you might not be able to sell it. Here's a last final reminder: You don't have to have a lot of cash to buy

property. You just have to know property values and know how to locate buyers to buy these properties from you. Some people have made a business of specializing in the earnest money option techniques. You can too, if it fits your style and needs.

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◀ *Technique 50:*
Lease with
an Option to Purchase

Those of you who do not own property now and are not able to finance your own home should go immediately to the "houses for lease" section of your paper and start looking for those types of property that are owned by an individual who may be willing to lease the house to a renter with an option to purchase in the future. You should try to locate someone who does not understand perhaps the value of his property or is willing to give you a long-term lease with the value of the property locked in in the future at a price that will give you an opportunity to make a profit from the option.

For example, you may locate a $50,000 house which might be worth $55,000 or $60,000 with a touch up, and the seller is willing to lease the property to you on a long-term lease, say two or three years with a three-year option to purchase for $72,000. In some areas, even in the periods of relaxed appreciation, it is not uncommon for properties to appreciate at anywhere between 10 and 15 percent per year on an average. Therefore, that house that you option today may be worth $85,000 in three year's time, whereas you have your price locked in at $72,000. The difference between $85,000 and $72,000 is a profit to you, and although you are renting the property for that three-year period of time, you are building up an equity in the profit that you make from the eventual option exercise.

(1) Credits Toward Purchase. It is customary in many of these situations to have the seller credit a certain percentage of your monthly payment towards the eventual purchase price; perhaps 25 percent of your $300 payment is credited in the future towards the purchase price of $72,000. This could be as much as $75 a month or maybe even as much as $1,000 a year. So that's another $3,000 that you may be able to reduce the purchase price by.

(2) Recording the Option. It's also customary that the option is recorded, and the seller can sell his property to any other individual if he so wishes. However, the new owner realizes that he is picking up the option on his property and has to honor it as the previous owner had to honor it. Usually in these option situations you will find a person who is really very concerned with making his monthly payment current and is not horribly interested in making a great amount of cash flow from his property. Therefore, you can negotiate a long-term lease whereby we promise to make his monthly payments for a long period of time without having a substantial rent increase, and you negotiate with him that you will take care of all maintenance items, that he will not have to do anything whatsoever.

(3) Lease with Option to Purchase Form. The lease with option to purchase form included here has many of these items already built into it. This is an added benefit because on this $50,000 house the fellow may have a $35,000 mortgage, and his mortgage payment is substantially less than the mortgage payment you would have to make if you were to buy his property for $50,000 with a $50,000 mortgage. Therefore, it eliminates the probability of negative cash flows, and since you are going to sub-let this property out to another tenant, you may be able to charge a higher rent and thereby have a positive cash flow coming in from your investment.

I know of several investors who have dozens of lease houses with options to purchase, and from these homes they generate for themselves a monthly cash flow which they use to supplement their investing. As each house gets ready for the option to be exercised, they can just go down to the bank and refinance it for the option price and pick up the property without having to invest any money.

RESIDENTIAL LEASE WITH OPTION TO PURCHASE

RECEIVED FROM.....hereinafter referred to as Tenant,

the sum of $.....(.....DOLLARS),

evidenced by....., as a deposit which, upon acceptance of this Lease shall belong to the Owner of the premises, hereinafter referred to as Owner and shall be applied as follows:

	RECEIVED	PAYABLE PRIOR TO OCCUPANCY
Rent for the period from..... to	$.....	$.....
Last..... month's rent	$.....	$.....
Security Deposit	$.....	$.....
Key Deposit.....	$.....	$.....
Cleaning charge	$.....	$.....
Other	$.....	$.....
TOTAL	$.....	$.....

In the event that this agreement is not accepted by the Owner or his authorized agent, within.....days, the total deposit received shall be refunded.

Tenant hereby offers to lease from the Owner the premises situated in the City of ....., County of ....., State of.....,

described as .....,

and consisting of.....

upon the following TERMS and CONDITIONS:

TERM: The term hereof shall commence on....., 19....., and continue for a period of.....months thereafter.

RENT: Rent shall be $.....per month, payable in advance, upon the.....day of each calendar month to Owner or his authorized agent, at the following address: ..... or at such other places as may be designated by Owner from time to time. In the event rent is not paid within five (5) days after due date, Tenant agrees to pay a late charge of $10.00 plus interest at 10% per annum on the delinquent amount. Tenant agrees further to pay $5.00 for each dishonored bank check.

UTILITIES: Tenant shall be responsible for the payment of all utilities and services, except:....., which shall be paid by Owner.

USE: The premises shall be used as a residence with no more than.....adults and.....children, and for no other purpose, without the prior written consent of the Owner.

PETS: No pets shall be brought on the premises without the prior consent of the Owner.

ORDINANCES AND STATUTES: Tenant shall comply with all statutes, ordinances and requirements of all municipal, state and federal authorities now in force, or which may hereafter be in force, pertaining to the use of the premises.

ASSIGNMENT AND SUBLETTING: Tenant shall not assign this agreement or sublet any portion of the premises without prior written consent of the Owner which may not be unreasonably withheld.

MAINTENANCE, REPAIRS OR ALTERATIONS: Tenant acknowledges that the premises are in good order and repair, unless otherwise indicated herein. Owner may at any time give Tenant a written inventory of furniture and furnishings on the premises and Tenant shall be deemed to have possession of all said furniture and furnishings in good condition and repair, unless he objects thereto in writing within five days after receipt of such inventory. Tenant shall, at his own expense, and at all times, maintain the premises in a clean and sanitary manner including all equipment, appliances, furniture and furnishings therein and shall surrender the same, at termination hereof, in as good condition as received, normal wear and tear excepted. Tenant shall be responsible for all repairs required for exposed plumbing or electrical wiring and for damages caused by his negligence and that of his family or invitees or guests. Tenant shall not paint, paper or otherwise redecorate or make alterations to the premises without the prior written consent of the Owner. Tenant shall irrigate and maintain any surrounding grounds, including lawns and shrubbery, and keep the same clear of rubbish or weeds, if such grounds are a part of the premises and are exclusively for the use of the Tenant.

ENTRY AND INSPECTION: Tenant shall permit Owner or Owner's agents to enter the premises at reasonable times and upon reasonable notice for the purpose of inspecting the premises or showing the same to prospective tenants or purchasers, or for making necessary repairs.

INDEMNIFICATION: Owner shall not be liable for any damage or injury to Tenant, or any other person, or to any property, occurring on the premises, or any part thereof, or in common areas thereof, and Tenant agrees to hold Owner harmless from any claims for damages no matter how caused.

POSSESSION: If Owner is unable to deliver possession of the premises at the commencement hereof, Owner shall not be liable for any damage caused thereby, nor shall this agreement be void or voidable, but Tenant shall not be liable for any rent until possession is delivered. Tenant may terminate this agreement if possession is not delivered within ..... days of the commencement of the term hereof.

DEFAULT: Any failure by Tenant to pay rent when due, or perform any term hereof, shall, at the option of the Owner, terminate all rights of Tenant hereunder. In the event that Tenant shall be absent from the premises for a period of 5 consecutive days, while in default, Tenant shall, at the option of the Owner, be deemed to have abandoned the premises and any property left on the premises shall be considered abandoned and may be disposed of by Owner in any manner allowed by law. In the event that Owner reasonably believes that such abandoned property has no value, it may be discarded. All property on the premises is hereby subject to a lien in favor of Owner, for payment of all sums due hereunder, to the maximum extent allowed by law.

Recovery of the premises by Owner shall not relieve Tenant of any obligation hereunder, and Owner may let the premises to others upon such terms and conditions as he deems proper, and recover from Tenant sums due hereunder, less any consideration received from others for the use of the premises, for the remaining term hereof, after paying expenses.

SECURITY: The security deposit set forth above, if any, shall secure the performance of Tenant's obligations hereunder. Owner may, but shall not be obligated to, apply all or portions of said deposit on account of Tenant's obligations hereunder. Any balance remaining upon termination shall be returned to Tenant.

DEPOSIT FUNDS: Any returnable deposits shall be refunded within two weeks from date possession is delivered to Owner or his Authorized Agent.

ATTORNEYS FEES: In the event that Owner shall prevail in any legal action brought by either party to enforce the terms hereof or relating to the demised premises. Owner shall be entitled to all costs incurred in connection with such action, including a reasonable attorney's fee.

WAIVER: No failure of Owner to enforce any term hereof shall be deemed a waiver, nor shall any acceptance of a partial payment of rent be deemed a waiver of Owner's right to the full amount thereof.

NOTICES: Any notice which either party may or is required to give, may be given by mailing the same, postage prepaid, to Tenant at the premises or to Owner at the address shown below or at such other places as may be designated by the parties from time to time.

HEIRS, ASSIGNS, SUCCESSORS: This lease is binding upon and inures to the benefit of the heirs, assigns and successors in interest to the parties.

TIME: Time is of the essence of this agreement.

HOLDING OVER: Any holding over after expiration hereof, with the consent of Owner, shall be construed as a month-to-month tenancy in accordance with the terms hereof, as applicable. No such holding over or extension of this lease shall extend the time for the exercise of the option unless agreed upon in writing by Owner.

PROFESSIONAL PUBLISHING CORPORATION

OPTION: So long as tenant is not in default in the payment of the rent provided for, Tenant shall have the option to purchase the real property described herein for a PURCHASE PRICE OF $.....(.....DOLLARS), upon the following TERMS and CONDITIONS:

ENCUMBRANCES: In addition to any encumbrances referred to above, Tenant shall take title to the property subject to: 1) Real Estate Taxes not yet due and 2) Covenants, conditions, restrictions, reservations, rights, rights of way and easements of record, if any, which do not materially affect the value or intended use of the property.

The amount of any bond or assessment which is a lien shall be ☐ paid, ☐ assumed by .....

EXAMINATION OF TITLE: Fifteen (15) days from date of exercise of this option are allowed the Tenant to examine the title to the property and to report in writing any valid objections thereto. Any exceptions to the title which would be disclosed by examination of the records shall be deemed to have been accepted unless reported in writing within said 15 days. If Tenant objects to any exceptions to the title, Owner shall use all due diligence to remove such exceptions at his own expense within 60 days thereafter. But if such exceptions cannot be removed within the 60 days allowed, all rights and obligations hereunder may, at the election of the Tenant, terminate and end, unless he elects to purchase the property subject to such exceptions.

EVIDENCE OF TITLE: Evidence of Title shall be in the form of ☐ a policy of title insurance, ☐ other:..... to be paid for by.....

CLOSE OF ESCROW: Within ..... days from exercise of the option, or upon removal of any exceptions to the title by the Owner, as provided above, whichever is later, both parties shall deposit with an authorized escrow holder, to be selected by the Tenant, all funds and instruments necessary to complete the sale in accordance with the terms and conditions hereof.

PRORATIONS: Rents, taxes, premiums on insurance acceptable to Tenant, interest and other expenses of the property to be prorated as of recordation of deed. Security deposits, advance rentals or considerations involving future lease credits shall be credited to Tenant.

EXPIRATION OF OPTION: This option may be exercised at any time after....., 19....., and shall expire at midnight ....., 19....., unless exercised prior thereto. Upon expiration Owner shall be released from all obligations hereunder and all of Tenants rights hereunder, legal or equitable, shall cease.

EXERCISE OF OPTION: The option shall be exercised by mailing or delivering written notice to the Owner prior to the expiration of this option and by an additional payment, on account of the purchase price, in the amount of

$.....(.....DOLLARS) for account of Owner to the authorized escrow holder referred to above, prior to the expiration of this option.

Notice, if mailed, shall be by certified mail, postage prepaid, to the Owner at the address set forth below, and shall be deemed to have been given upon the day following the day shown on the postmark of the envelope in which such notice is mailed.

In the event the option is exercised, ... percent from the rent paid hereunder prior to the exercise of the option shall be credited upon the purchase price.

The undersigned Tenant hereby acknowledges receipt of a copy hereof.

.....Agent — DATED:.....

By:..... — .....Tenant

Broker:..... — .....Tenant

.....Address — .....Address

.....Phone — .....Phone

ACCEPTANCE

The undersigned Owner accepts the foregoing offer.

BROKERAGE FEE: Upon execution hereof the Owner agrees to pay to .....,
the Agent in this transaction, the sum of $.....(.....DOLLARS)
for leasing services rendered and authorizes Agent to deduct said sum from the deposit received from Tenant. In the event the option is exercised, the Owner agrees to pay Agent the additional sum of $.....(.....DOLLARS).
This agreement shall not limit the rights of Agent provided for in any listing or other agreement which may be in effect between Owner and Agent. In the event legal action is instituted to collect this fee, or any portion thereof, the Owner agrees to pay the Agent a reasonable attorney's fee and all costs in connection with such action.

The undersigned Owner hereby acknowledges receipt of a copy hereof.

DATED:.....

.....Address — .....Owner

.....Phone — .....Owner

The detriments, of course, are that you have to be a manager of your units and make sure they are taken care of. You also do not get the benefits of a tax shelter or equity build-up or the total amount of the appreciation, but you do get to pick up long-term appreciation and cash flow. I know of one investor who has approximately 30 to 35 of these lease with option to purchase houses, and this is his full-time job. He spends all his time managing and leasing out his houses and earning the benefits that come from the cash flow and long-term appreciation.

A note to the wise: If properties in your area have not been following a pattern of healthy and attractive appreciation in recent times, it does not mean that the lease-option technique will not work for you. It simply means that you will want to be doubly careful to find properties that can be locked into a *discounted* price. This way, you can make your profit "going in" to the transaction and do not need to speculate on future appreciation. In fact, it is smart for all of us to structure our lease-option deals in such a way that we can win without gambling on property appreciation. In that way, if properties do appreciate beyond our expectation, it's all cream!

Creating Wealth

WITH LITTLE OR NOTHING DOWN

Manual

The Nothing Down System of Creative Financing in Real Estate Investments

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SECTION Q

Conversions

Robert G. Allen

M.B.A.

IN COOPERATION WITH

Richard J. Allen

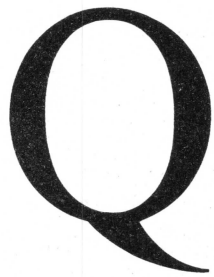
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Conversions



A. THE THEORY BEHIND "BORN AGAIN" PROPERTY..... Q- 3
B. SOME EXAMPLES..... Q- 3
1. The Fixer Upper ..... Q- 3
2. Apartment to Office Building ..... Q- 4
3. Apartment to Condominiums: The Wave of the Future..... Q- 4
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Conversions



A. THE THEORY BEHIND "BORN AGAIN" PROPERTY

One of the hallmarks of the creative thinker is the ability to envision new and unconventional uses for things—to see things in patterns of productive usage that are not readily discernible to the average person.

The creative investor always perceives a property not just for what it is but for what it might *become.* The process of *converting* a property to a different or higher usage has enormous profit potential. Consider these typical ground costs:

Raw undeveloped land ..... as little as $100 per acre
Farm ground ..... $2,500 per acre or more
Subdivision land ..... $25,000 per acre or more
Apartment ground ..... $75,000 per acre or more
Shopping center and
office building ground ..... $250,000 per acre or more

To cross the threshold from one type of land usage to another creates a great potential for the pyramiding of values. The chart overleaf will illustrate this phenomenon.

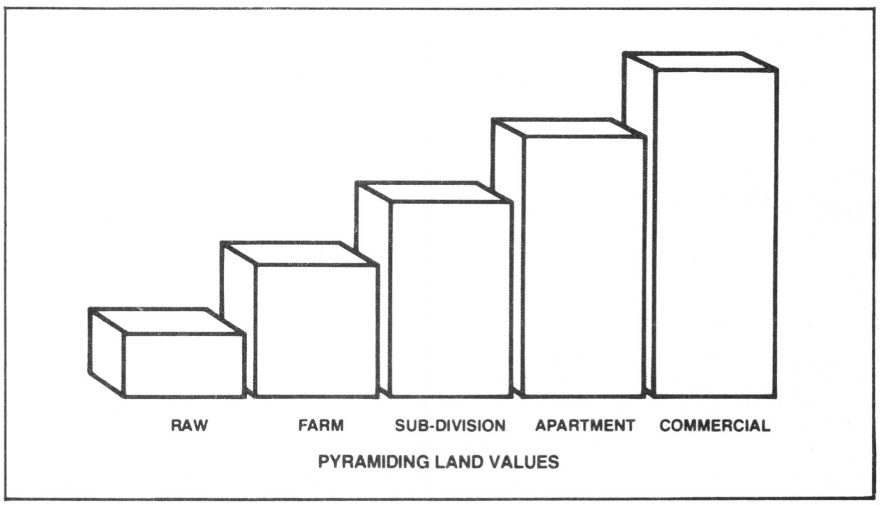
B. SOME EXAMPLES

Profits in conversions can be enormous, but the process can be complex and challenging. A keen sense of market and development patterns, together with courage and financial creativity are musts. Here are some examples, beginning with an easier one:

1. The Fixer Upper

There are bright possibilities, even for the enterprising beginner, to transform run-down properties into livable and attractive units and hence increase their value greatly. This is the simplest conversion of all. The best book available on this subject is William Nickerson's *How I Turned $1,000 into Five Million in Real Estate: In My Spare Time,* Rev. ed., published by Simon and Schuster.

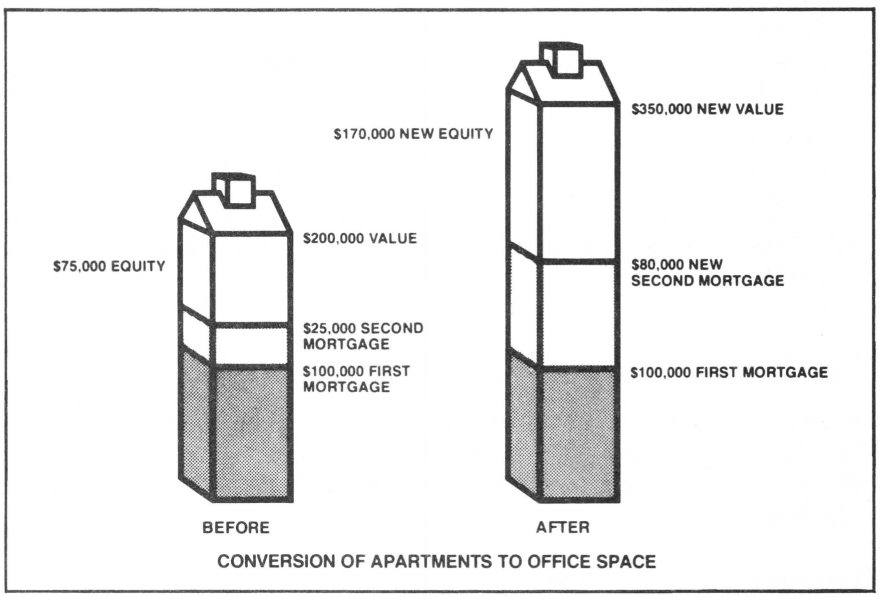
Before the conversion, the apartment building had a net operating income of $12,600. With a cap rate of 7 percent, the value of the apartment building would be around $180,000 ($12,600 ÷ .07). However, as a 9,000 square foot office leased out at $7.00 per square foot, the net operating income turns out to be $37,860 (60 percent of the gross operating income of $63,000). Thus, the value is increased to around $500,000 ($37,860 ÷ .07). Moreover, there is now a breakeven cash flow.



PYRAMIDING LAND VALUES

2. Apartment to Office Building

The following sketch illustrates an actual case:



CONVERSION OF APARTMENTS TO OFFICE SPACE

3. Apartments to Condominiums: The Wave of the Future

Some possible advantages:

a. Down payments from new buyers of the units can nearly cover the down payment you make for the building and most of the conversion costs.

b. A substantial positive monthly cash flow is possible when the financing for the condo units is done by you (the new owner) in the form of paper carried back after down payments.

c. More likely than not, actual physical improvements will be minimal.

d. You will be catering to the needs of people to own their own homes in an era where increasingly fewer can afford individual homes.

4. Land Subdivisions

Where an astute buyer has done his homework, checked the patterns of commercial development in the community, checked zoning, checked for

utilities, reviewed market conditions carefully, etc., the following can happen with an illustrative ten acre parcel of land:

Land costs at $25,000 per acre	=	$ (250,000)
Less: Development costs of $5,000 per lot (total lots = 30)		(150,000)
Miscellaneous costs at $1,000 per acre		(30,000)
Total expenses		$ (430,000)
Sales of 30 lots at $20,000 each		$ 600,000
TOTAL PROFIT		$ 170,000

You can still open a gold mine without mining gold!

Creating Wealth

WITH LITTLE OR NOTHING DOWN

Manual

The Nothing Down System of Creative Financing
in Real Estate Investments

SECTION R

Exchanging

Robert G. Allen

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Exchanging

R

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Exchanging

R

Exchanging is an extremely powerful field that is little known to the average investor. Yet, it is one of the most powerful ways of pyramiding your assets into a fortune. And, it's the best way to defer paying taxes.

A. NONTAXABLE ASPECTS OF EXCHANGING

A nontaxable exchange is an exchange of property in which the gain or loss is not immediately recognized for tax purposes. Recognition of the gain or loss is therefore *postponed* for the time being. Nontaxable exchange, therefore, implies tax postponement, not tax exemption. The following transactions can be nontaxable:

(1) Exchange of like property held for productive use of investment (i.e., business property, such as rental real estate).

(2) Involuntary conversions, such as condemnations.

(3) Sale or exchange of residence and repurchase of another residence.

Under the U.S. Installment Sale Revision Act (effective date October 19, 1980; P.L. 96-471), the regulations governing installment sales are considerably liberalized, making it easier than before to obtain important tax advantages in real estate exchanging. Check with your accountant for details. Note also, that in Canada the laws governing the tax aspects of exchanging are similar to those in the United States except that there is no tax on a gain realized from the sale or exchange of a personal residence.

There are *four basic tests* of a nontaxable exchange:

1. The Exchange Must Be "Like for Like" Property

Property of a like kind refers to the nature, character, or class of the property and not to its grade or quality. Thus, real estate, whether improved or unimproved, is property of like kind. The existence or lack of improvements merely affects its grade or quality. Nor does the location of the property matter. Thus, a ranch in the U.S. and a ranch in another country are like kind properties. Like kind refers to intent. Are they both investment properties? Like kind does not refer to a personal residence. But a personal residence may be converted into investment property when there is an appropriation of the property to rental purposes. A sign in the window advertising the property for rent may be sufficient.

2. No Boot Can Be Received

Boot is anything other than real estate—cash, the payment of debt, notes, personal property. If there is boot involved, it is taxable up to the value of the boot and is thereby not a part of the tax deferred exchange.

3. No Mortgage Relief Must Be Given

The amount of the mortgage to be assumed must be greater than the mortgage that is given up. Any difference is taxable much like boot.

4. Higher Valued Property

The property to be acquired must be more valuable than the property being disposed of.

Obviously, only one party to an exchange can have a tax-deferred status. It is, therefore, critical to have expert advice. Even these simple comments here should only be used to give a framework for understanding exchanges. If you are planning to execute an exchange, *do not—repeat, do not—proceed without the advice of an accountant trained to handle exchanges.*

B. TYPES OF EXCHANGES

1. Tax-Deferred Exchanges

This is an excellent way to preserve investment capital. And it is perfectly legal. As you become familiar with your multiple listing book, you will notice that many investment properties are advertised for sale subject to a 1031 exchange. Section 1031 in the U.S. Internal Revenue code refers to tax-deferred exchanges.

2. The Don't Wanter Exchange

The other type of exchange is a don't wanter exchange. The seller has a problem and is willing to be flexible enough to take anything to get out of his problem. He might exchange for land or for notes or whatever just to solve his problem.

C. EXCHANGES GROUPS

Both of these exchanges are handled most professionally by a society of exchange counselors in your area. In almost every state in the U.S., exchanging is beginning to become more and more popular among real estate agents. A current listing of all the exchange groups and their leaders in each state is available in the monthly publication *Creative Real Estate Magazine* (Box 2446, Leucadia, CA 92024). You can also obtain current information from your local Board of Realtors. An exchange group is a group of Realtors dedicated to solving client problems through exchanging. They meet at least once a month for brainstorming sessions. In many cases, properties change hands right at the meeting. In some cases these groups may not be formally organized; ask local real estate agents about exchange practices and exchange groups in your area.

1. Exchanger's Jargon

It is from exchanging that many of the words that I have used throughout the seminar have originated. A *don't wanter* is an exchange client who is willing to be flexible. A *cranker* is a property that can be refinanced to generate cash. A *swinger* is an individual who will take on almost any problem and solve it for a profit. *Cold storage* land is land that is only good for holding the world together but is an excellent way for a client to move out of management problems and reassess his position.

2. How to Get Involved

If you have a piece of property or if you have a problem property, an exchange counselor in your area would be more than happy to help you and counsel you in your problem. He can locate a new property to exchange into by contacting his exchange colleagues at the next exchange meeting. You can find a competent exchanger by contacting your local Board of Realtors and asking whether there is an exchange group that meets locally and, if so, who the president of the exchange group is. It is a real experience to be invited to attend an exchange meeting. If you can, attend one and see how property is exchanged.

D. THE PHILOSOPHY OF EXCHANGING = EVERYONE WINS

Since many of you will be involved in the future with trading your equities for other properties, let's go through some preliminary discussion on a two-way exchange and a three-way exchange and get you the feel for some of the philosophies that are involved therein.

The philosophy of exchanging is that people are more important than property. Most of the time when a property is sold, it is because of the person's problem and not the property's problem. If I am going to trade my property for yours, I am looking for certain benefits, and you are looking for certain benefits. If I need your benefits and you need mine, then it is a good exchange. There are no good one-sided exchanges.

1. A Two-Way Exchange

◀ *Technique 16:*

16

Let's suppose a builder has a house that he has just completed; it has a $10,000 equity in it, and he needs to sell his property to get the cash to buy another piece of land. If he sells his property for cash, he has to go out and find a cash buyer; he has to close on the transaction, take his cash, and use it to buy another building lot. On the other hand, suppose you have a lot that you own, and you decide not to build on it. You have decided to buy an investment house instead. Now wouldn't it make a lot more sense to try to arrange an exchange between you two and save an awful lot of time and energy since both of you are looking for each other's benefits. The builder doesn't want the house; he wants your land. You don't want your land; you want an investment house, something with more leverage. By exchanging, each of you moves to a better position with less expended energy.

You might find a fellow who has a 12-unit apartment building and can't stand the management. He says, "Give me a piece of free-and-clear bare ground that can sit there without causing me management headaches." On the other hand, a person with a large piece of vacant ground might find himself being eaten alive by taxes because he doesn't have any tax shelter. Can you see how both of these people could enter into an exchange and improve their positions considerably? This is what a two-way exchange is all about.

2. "I'm Going Up; He's Coming Down"

Many of you will be purchasing homes and small apartment buildings, and you will soon find that you will have an increase in equity in your property, and in order to gain increased leverage or a better use for your large equity, you will need to exchange into larger properties. Perhaps you have a duplex with $30,000 equity and want to trade into an eight-unit building. Why would someone with an eight-plex consider your offer to exchange? It may be easier to dispose of a duplex. A duplex may be easier to finance. He may still want to rid himself of negative cash flows he cannot handle. He wants more security. You can see how the benefits theory really works.

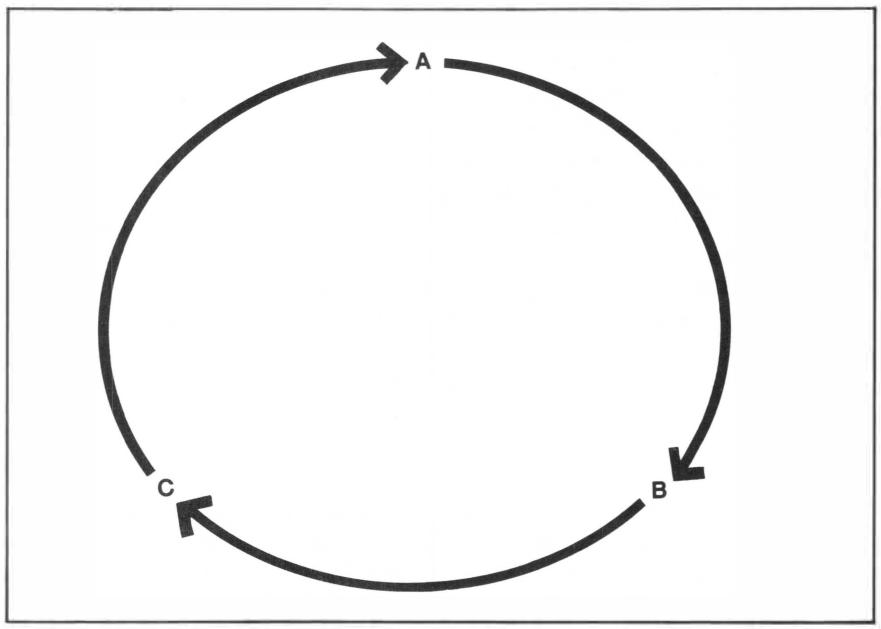
3. A Three-Way Exchange

◀ *Technique 17:*

17

A three-way exchange enters in the picture when you, with your duplex and $30,000 equity, find an eight-unit apartment that you like, but the eight-plex owner does not want your duplex. A wants B, but B does not want A.

[1]See the chart at the end of Section O to relate Techniques 16–18 to the already-discussed series of techniques.



The Three-Way Exchange

In that case, we are going to try to find a C that B will accept. If we do, C will have to want A, or we will have to find a D to complete the circle. You can see that some exchanges can get complicated.

E. THE DON'T WANTER REAL ESTATE AGENT

A lot of don't wanters are created out of multiple exchanges when the real estate agents involved are forced to take the first leg of the exchange (A) in order to complete an exchange that is endangered. Their commissions are paid by giving the real estate agents one of the properties in the multiple exchange. Obviously, the real estate agents usually don't want the property they have just acquired. They would rather have cash or cash flow from notes. In this way, it is possible to buy properties from these exchangers with nothing down—only paper. This is called "papering" a property. I have found several good properties by dealing with exchangers. They understand flexible and creative financing and are more prone to accept it.

F. LEMONADING

Technique 18: ▶ 18

One of my very first exchange clients was a couple who had purchased a piece of speculative real estate years before. It was more a swindle than an investment, and they had experienced little appreciation. What's worse, the property had been up for sale for more than a year with no success. They came to me wanting to see if there wasn't some way to move the $19,000 equity in their land into something more attractive.

I came up with a quick solution by suggesting that they refinance their house and add the proceeds of $30,000 to the equity in the land; with $49,000 equity composed of land and cash, they might have a better chance of moving their problem property.

I made a trip to Phoenix to a real estate exchangers' meeting, and within two days I had 20 or 30 offers to trade for the property. I quickly learned that when a little cash is involved, people pay attention. Lemon plus sugar makes lemonade. Add sugar (cash) to your sour investments (lemons) and see how fast they go!

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SECTION S

Summary – Putting Into Action

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Summary: Putting the "Nothing Down" Program into Action



A summary of the seminar's basic challenges:

1. Reread the entire manual again. Get a feel for the techniques.

2. Prepare your financial statement.

3. Fill out your goal commitment sheet and hang it in a prominent place for daily reading. *Don't skip this step. Everything hinges upon it!*

4. Clear up your short-term obligations. Pay off debts which cause high monthly obligations. Tighten your purchasing of non-appreciating assets. Prepare your budget for some negative cash flow. Clear up your credit if possible. Start an emergency fund.

5. Obtain copies of the books mentioned in the bibliography and study them.

6. Practice the creative attitude in all aspects of your life—defer judgment, think positive, be a solution to the problem instead of part of the problem.

7. Begin your search for the don't wanter. Choose several approaches and start to concentrate. You've got to circulate if you want to percolate.

8. Begin reading your local newspaper at least once a week in depth. Make short-term goals:
- Call twenty ads per week
- Inspect two properties per week
- Make one offer every other week
- Make time for consistent searching. Select a regular time and stick to it.

9. Contact several Realtors about your goals. Visit one new office per week. Begin to learn how to study a Multiple Listing Service book.

10. Practice your seller analysis by stopping at a for-sale-by-owner and testing out the questions on him. Remember that if he is not a don't wanter, he may not respond. Don't worry! It's just practice anyway, and it might lead you to your first purchase.

11. Visit several financial institutions and find out who is making non-owner occupied loans. What are the terms? What qualifications does one need? Become familiar with the money market.

12. Find your partners. Your goal is $25,000 in cash.

13. Locate people who invest in discounted second trust deeds (mortgages). Find out their guidelines. Prepare yourself to use their service.

14. If possible, attend an exchange meeting to get the feel of how property is exchanged.

15. Visit three to five banks in your area. Make application for (1) loans and (2) MasterCard and VISA.

16. Establish relationships with the professionals. Sooner or later you're going to need them.
- Attorneys
- Accountants
- Title companies (U.S.)
- Property rental and management companies
- Appraisers
- Bank and loan officers
- Real estate agents
- Local zoning and planning officials
- A local building contractor
- An inspection service
- A well-known and successful real estate investor

Most initial visits will be free. You'll be surprised how the fear will dissipate once you remove the *high-powered titles* and stick people's *names* and *faces* in their place.

17. Find out which rules of thumb your area uses in doing financial investment analysis. Call on a few properties in the paper or in the MLS book. Perform your cap rate analysis. Practice, practice, practice!

18. Know what your market is!

19. Obtain some Earnest Money Agreements (in Canada, Interim Agreement and Offer to Purchase). Make an offer on a property you pass by on the way to work. Get the feeling for what it is like to be turned down for presenting a "creative" offer. It won't be the first time—or the last.

20. Remember patience! You must learn to temper the motivation part of this course with persistence. Relax. All will fall into place in time. For some of you it will be feast from the very start. For some of you it will be famine. Be prepared to wait it out if necessary. And don't gorge yourself at feast time either. If you are buying too many properties, you are not a very good negotiator.

If you can buy just one property each year, you're doing fine!
If you can buy two, that's fantastic!
If you can buy three, you have my admiration as well as the respect of all your fellow graduates.
God Bless You.

Sincerely,

Robert G. Allen

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SECTION T

Epilogue - Fear

Robert G. Allen

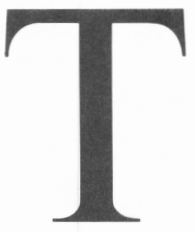
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Epilogue— Fear: The Thief of a Happy and Successful Life



1. As to the Confused and Negative Mind ..... T- 3
2. As to the Paralysis of Analysis ..... T- 3
3. As to Conservatism ..... T- 3
4. As to the Fear of Asking for What You Want ..... T- 4
5. As to the Fear of a Failing Economy ..... T- 4
6. As to Procrastination ..... T- 5

"A Reluctant Investor's Lament" (A Poem)..... T- 5

Epilogue— Fear: The Thief of a Happy and Successful Life

This seminar has given you what you need to achieve financial independence. With the knowledge and skill gained through practice, there is nothing that can prevent you from acting to achieve your goals, except *fear.*

Fear is the basis for failure. Fear underlies the six major reasons why people don't succeed.

(1) A confused mind always says "No."
(2) The paralysis of analysis.
(3) The overly-conservative investor.
(4) Fear to ask for what you want.
(5) Fear the economy will fail.
(6) Procrastination.

To some extent, all of us experience fear in varying degrees. The object is not to eliminate fear but to resist it and master it.

"Courage is resistance to fear,
mastery of fear—not absence of fear."
—Mark Twain

How can you master fear and overcome inertia? Let us look at the positive side and enumerate some solutions.

1. As to the Confused and Negative Mind:

Solutions:

- Study the "Nothing Down" system carefully.
- Organize your thoughts and goals.
- Add confidence to your competence.
- Talk with those who have achieved success.
- Avoid accepting false evidence that "things won't work," even if it appears on the surface that the evidence might be real.
- Get out and get your feet wet!

2. As to the Paralysis of Analysis:

Solutions:

- Knowledge and analytic thought are essential—until you start using the need for them as an excuse for not acting.
- You don't need a Ph.D. to succeed, but you do need a D.S.C. (Doctor of Common Sense) and a D.A. (Doctor of Action).
- Get the knowledge you need, think things through, and then get out and *do* something!

3. As to Conservatism:

Solutions:

- There is an essential place for conservatism in the "Nothing Down" system:
  —It is conservative to develop an orderly and coherent game plan.

—It is conservative to analyze properties with caution and exactness.

—It is conservative to learn the precise details of the seller's position and circumstances.

—It is conservative to structure the financing so as to avoid negative cash flows and receive the greatest possible return on your investment.

—It is conservative to be familiar with the widest variety of options and techniques for preserving and maximizing your investment.

- In fact, the "Nothing Down" System is a unique combination of conservatism, creativity, competence, and courage.
- What must be avoided is the type of conservatism that breeds inertia and inactivity. This is the conservatism of fear. We live in a new era of investments. The leverage principle emerged in a broadly based way only in the late 1950s and early 1960s. Old conservative approaches are inadequate to the times.
- *The greatest risk of all is to be so conservative that you fail to invest at all.*

4. As to the Fear of Asking for What You Want:

Solutions:

- It is amazing what people will do if you only ask.
- When carrying out investment activities, ask sincerely and confidently with a high measure of interest in the other person. All he or she can say is "No." And if you ask politely, the answer might even be "No, thank you." That response never hurt anyone.
- Look upon it as a profitable enterprise in which everyone wins. You are asking the other guy to let you help him solve his problem:

  —The loan officer needs to make money in interest. Help him.

  —The don't wanter seller needs to divest himself of the property. Help him.

  —The holder of the underlying mortgage needs to improve his position. Help him.

  — Your partner needs to make a profitable investment. Help him.
- Ask questions which help people solve their problems. And you solve problems at the same time. You'll never know until you ask.

5. As to the Fear of a Failing Economy:

Solutions:

- Look at the probabilities realistically. What are the chances for a bust? Ten percent? Twenty percent? Twenty-five percent? What is the probability that real estate will continue to increase in value barring a major economic crash? Eighty percent? Ninety percent? One hundred percent? Will inflation continue to plague us? If so, real estate will continue to go up. You decide where you like to place your money.
- What are the alternatives?

  (a) Put your head in the sand and wait.

  (b) Invest with prudence and creativity.
- What are the implications of these two choices?

  (a) If the economy makes it (as it will!)

  —The head-in-the-sander has got his pittance.

  —The "Nothing Down" investor has his financial independence.

  (b) If the economy busts (as it won't!):

  —The head-in-the-sander loses all. (With his fairly high equity, guess whose home the bank will foreclose on first?) If not, do you think he will have the experience or courage to invest at the bottom of the market to take advantage of his preserved capital?

  —The "Nothing Down" investor loses what he put in in the first place—

nothing! And if he has been wise, the "Nothing Down" investor will have arranged his portfolio to have a home and some investment properties free-and-clear in order to enjoy a comfortable living while he waits for the economy to recover. (Even Howard Ruff believes that the economy will recover!) When that happens, he is far ahead of the head-in-the-sander, for he has his knowledge, courage, and creativity and can start all over again—with a period of low prices and lots of don't wanters.

6. As to Procrastination:

Solutions:

- Consider the consequences of your inaction. If you do nothing, you are using the "Nothing Done" system, and these are the results:
  —Perpetual end-of-the-month blues.
  —Punching the clock for the rest of your life.
  —Fighting traffic and congestion.
  —Scraping for every penny.
  —Eternally putting off what you really want to do (write that novel, study art, raise horses, learn to fly, take the family around the world, study law, whatever!).
- Set realistic goals and accomplish them one by one. Eat the elephant one bite at a time.

As a final note, remember that you either pay the price now and enjoy the rest of your life doing what you want to do or you can pay the price later, which may mean living your declining years with a declining income. Don't make the wrong choice.

"The money which a man possesses
is the instrument of freedom."
—Rousseau

A RELUCTANT INVESTOR'S LAMENT

I hesitate to make a list
Of all the countless deals I've missed;
Bonanzas that were in my grip—
I watched them through my fingers slip;
The windfalls which I should have bought
Were lost because I overthought;
I thought of this, I thought of that,
I could have sworn I smelled a rat,
And while I thought things over twice,
Another grabbed them at the price.
It seems I always hesitate,
Then make my mind up much too late.
A very cautious man am I
And that is why I never buy.

When tracks rose high on Sixth and Third,
I thought the price asked was absurd;
Whole blockfronts—bleak and black with soot
Were priced at thirty bucks a foot!
I wouldn't even make a bid,
But others did—yes, others did!
When Tucson was cheap desert land,
I could have had a heap of sand;
When Phoenix was the place to buy,
I thought the climate much too dry;

"Invest in Dallas—that's the spot!"
My sixth sense warned me I should not.
A very prudent man am I
And that is why I never buy.

How Nassau and how Suffolk grew!
North Jersey! Staten Island, too!
When others culled those sprawling farms
And welcomed deals with open arms . . .
A corner here, ten acres there,
Compounding values year by year,
I chose to think and as I thought,
They bought the deals I should have bought.
The golden chances I had then
Are lost and will not come again.
Today I cannot be enticed
For everything's so overpriced.
The deals of yesteryear are dead;
The market's soft—and so's my head.

Last night I had a fearful dream
I know I wakened with a scream:
Some Indians approached my bed—
For trinkets on the barrelhead
(In dollar bills worth twenty-four
And nothing less and nothing more)
They'd sell Manhattan Isle to me.
The most I'd go was twenty-three.
The redmen scowled: "Not on a bet!"
And sold to Peter Minuit.

At times a teardrop drowns my eye
For deals I had, but did not buy;
And now life's saddest words I pen—
"If only I'd invested then!"

You don't steal in slow motion!

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SECTION U

The Final Word

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The Final Word: Creative Self-Unemployment

U

A. WHAT IT'S LIKE TO BE FREE

If you could do anything you wanted to do right now, for the rest of your life, what would it be? Would you golf, would you read, would you write, would you help underprivileged nations, would you work in your church, give your time to charity, die of boredom; what would it be? What I hope you understand is that if you follow the program that we outlined in this seminar point by point, detail by detail, somewhere between the fifth and tenth year of your following this program, you will be able to spend the rest of your life doing the kinds of things that are important to you. You will be able to be your own boss, to do your own thing. No longer will you have to push someone else's pencil; no longer will you have to worry about the alarm clock waking you up early in the morning and having to jump out of bed and run off to work and say, "Yes, sir" and "No, sir." You will be able to say, "I do what I want when I want; I am my own boss."

This is a powerful feeling. This is what it is truly like to be free, especially free from financial bondage. This is yours if you follow the program. If you'd like to do it quicker, if you would like to quit your job in less time than what we have outlined here, say in less than five years, you will have to make some sacrifices. And there are some very important rules that you should never break. There are benefits that come from being your own boss. One is the ability to handle your own time.

B. THE PROBLEMS OF BECOMING FINANCIALLY INDEPENDENT

And there are also some detriments, and let's talk about that.

1. The Loss of a Steady Cash Flow

First of all, you have no longer a cash flow to rely upon. Once this habit is broken and you don't have a steady income coming in, things can get rather hectic for a while.

2. Vanishing Credit

This additional cash flow which is also coming in steadily also gives you the ability to be able to borrow money from a bank, and once you quit your job, you become what they call self-employed or what I refer to as self-unemployed. Because you have very little ability to borrow money, the only way they'll lend you money is if you can prove over a consistent period of three or four years' time that you are a good money risk.

3. Lack of Fringe Benefits

You also lose all the benefits that a company provides, such as job training and the golden handcuffs such as insurance benefits and attorney benefits and retirement benefits and employer/employee matching Social Security (social insurance) benefits, etc. All these things are now gone, and you are on your own.

C. ATTAINING CREATIVE SELF-UNEMPLOYMENT

Having lived under this system almost all of my life where I am the only person to whom I am responsible, I find it exhilarating; I find it very scary sometimes. I find it sometimes hard to motivate myself to get going, but I am my own boss, and that is one of the most important things that I can be.

1. Maintaining a Sense of Destiny

A ship in a harbor is safe, but that is not what ships were built for. They were built to be on the high seas, to be carrying cargo from place to place. It is my personal opinion that we came to this earth to do great things, and we can't do great things if we are constantly worrying about money. We can't do great things if we have to be driven each day to do our jobs to work at things that we do not enjoy doing, to come home mentally, physically, and spiritually fatigued, not having enough energy to do the kinds of things we know we need to do to contribute to the society which we believe in, too tired to help others, with only enough energy to watch *The Tonight Show* and to go to bed and get enough rest so that we have enough energy to go back and to do the kinds of things we hate to do the next day. This is not financial independence. "Man is that he might have joy." This is not joy. If you are going to work, work at something that you love to do. If you must be involved constantly, do something that is fulfilling. Five years from this very moment, if you do the things we ask, you will be doing those things that are fulfilling to you. It may be very hard work, but it will be very worthwhile and important.

2. Before You Quit Your "Ho-Hum" Job

One thing you must remember is that you must be very careful about quitting your job and investing in real estate on a full-time basis until you are prepared.

a. Basic Needs: Experience, Borrowing Power, Equities. There are a few kinds of things that you need to take into consideration. Number one, you have to have the experience. Number two, you need to have the borrowing power established with the banks before you quit. Number three, you need to have some kind of equities accumulated from which you can generate needed cash if necessary.

b. The Key: Accumulating Real Estate, Not Selling It. You must be careful about trying to generate income from your real estate investment because you will find that more often than not you will be forced to sell your real estate holdings just to keep yourself going on a day-to-day basis, and that is the antithesis of your investment program. Your investment program is the accumulation of real estate, not the selling of it for living expenses.

c. Stick with It or Switch Jobs. Therefore, I recommend that you remain in your job, whether you like it or not, or transfer to a job that you can relate to or you can enjoy or a job that gives you more of an opportunity to learn more about real estate. If we invest our time and our money wisely, in five years we will be able to do anything we want to do with our time and with our money. But if you don't invest it wisely now, you will never be able to have the opportunity to do so.

d. First Build Up Reserves. Have at least six to 10 months' cash or living commodities stored up before you ever quit a job. You can imagine how embarrassing it would be if you had gone to your boss and told him to drop dead and then had to come back to him crawling on your hands and knees six months later to tell him that you couldn't make it in the big, bad world, and you had to come back into the secure fold. If you only have the courage to break away from the normal ways of society once, make sure that when you do your break away that it's clean and neat, and you never have to be tempted to

go back to work to do something that you don't want to do. That is demoralizing; that is not the kind of thing that causes financial independence and confidence.

D. GENERATING CASH FLOW FROM REAL ESTATE

There are five ways to generate cash flow from your real estate.

1. Turning Around "D" Properties

Buy properties in D areas on your concentric circle. Turn them around quickly; paint them if necessary; buy them with very small down payments, creative terms if possible; turn around and sell them with nothing down and create a $5,000 or $6,000 or $10,000 equity profit for yourself with a $50 or $100 cash flow override to yourself. This being five or six or 10 times over a period of two or three years could generate a $700 or $800 or $900 a month positive cash flow, which could be just the right kind of cushion for you to be able to quit your job and devote full-time to your investing.

2. Fixer Upper

Approach the problem of investing in real estate with the Nickerson attitude, which is the fix-up approach. Fix the property up which you have bought with minimal investment; make it nicer, create value, increase rents if necessary, then turn and sell for cash, enough cash to generate a profit for yourself to regenerate a down payment for the next investment and to give you enough money to live on for the next two or three months until you can sell your property again. The only type of problem with this type of program is that sometimes it takes the time and energy away from your accumulation program. You should always try to buy a piece of property for long-term holding every time you sell a piece of property on which you have made a short-term profit. It's the accumulation of real estate holdings which makes a person wealthy, not the selling of them. You don't want to kill the goose that lays the golden egg. You want to keep that goose and make that goose happy.

3. Become a Real Estate Agent

My first three years out of college were spent in the real estate industry learning all the ins and outs of the real estate world and making commissions on the side. I soon came to a point in my career where I decided that I was making more money in my investing on my own portfolio than I was in helping clients, and I phased out of the real estate business and dropped my license altogether.

a. Benefits. A real estate job has several benefits. It gives you first crack at real estate listings, it allows you the opportunity to use your commission as a down payment for investment properties for yourself, it gives you a good working knowledge on how the real estate industry works, and teaches you how the marketplace reacts to certain events.

b. Drawbacks. However, there are detriments. First of all, there is the stigma that is attached to real estate agents. Most sellers do not like to deal with agents because commissions are involved. Many times the sellers like to sell their property without having the aid of an agent. The agent must disclose to the seller that he is a real estate agent and has to put this on his deposit form or earnest money agreement, and many times this taints the transaction in such a way that the seller does not want to sell. This is especially true if you seem to be a real estate professional and offer a lot of creative transactions. The sellers are less likely to accept these transactions if they feel you are perhaps taking advantage of them.

In addition to that, there is the liability. If you do accept the commission and use it as a down payment to buy a piece of property, the seller may change his mind in the future and come back and sue you for having taken advantage of him at a time when he was vulnerable. This, coupled with the

liability, is one of the main reasons why I dropped my license and find that I get just as much benefit from using other agents and paying them their commission as I would get by doing this by myself.

You will also find that working with real estate agents becomes much easier once they find that they are going to be paid a full commission without having to split their commission with you if you hold a real estate license.

4. Specialized Techniques

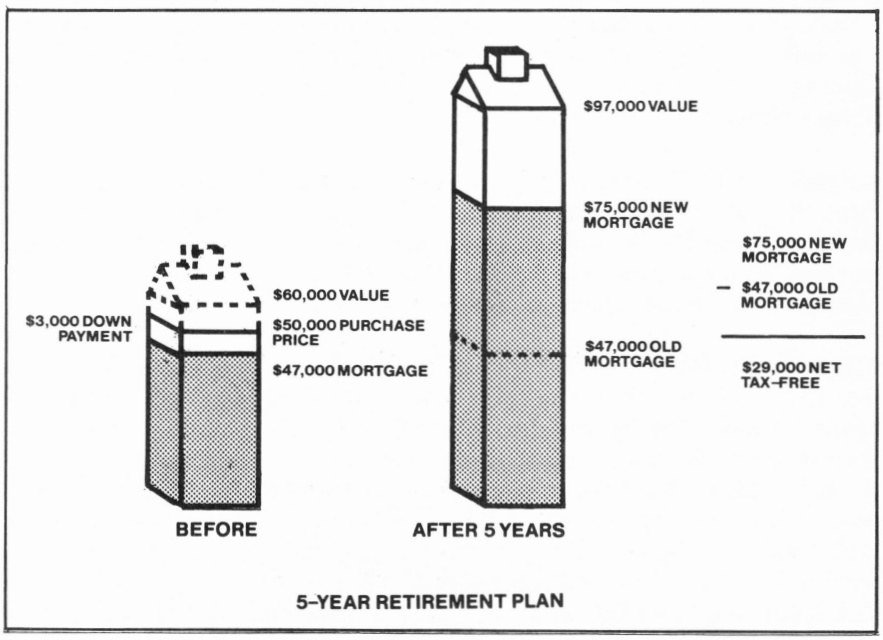
The fourth area of generating cash flow from real estate is the little known techniques we talked about throughout the seminar, the earnest money option approach for deals you can't handle yourself and the lease with option to purchase cash flow technique. Each of these may take as much as two or three or four years to generate enough cash flow coming in to make you feel comfortable with your ultimate freedom, but if you plan for it with full purpose of mind, you will become financially independent.

5. The Five-Year Retirement Plan

The last area of generating cash flow is for property owners only—the five-year retirement plan with homes.

Suppose you were able to devote one full day a week, say Saturdays, to looking for real estate investments. Since you have 52 Saturdays a year, you should be able to find and purchase just one property, one small home valued near $60,000, from a seller who is anxious to sell and will accept a $50,000 price with a $3,000 down payment. This will take some looking, but remember you have a year to find it. When you find the right property, buy it. If necessary, borrow the down payment, using one of the creative methods discussed earlier in this book. Then rent the house. (If you can't find such an inexpensive home in your area, locate the least expensive three-bedroom house you can find with the smallest down payment and the lowest negative cash flow. You don't have to use my numbers above, just follow the principle.)

For property owners only—the five-year retirement plan with homes



The next year, do exactly the same thing. Buy just one property valued below market price with a small down payment. Again, rent the house. You'll have to be able to rent the house for enough money to cover mortgage

payments, including taxes and insurance. The tenants will pay all utility bills and minor maintenance bills. In the first year or so the rental income will be tight, but after several years, you will begin to experience a steady positive cash flow.

In the third year, do the same thing. And so on until the fifth year when you'll own five rental homes, all rented out, with no negative cash flow. If you have chosen the property well, there is a good chance that it will appreciate considerably in a five-year period. Assuming 10 percent growth, let's look at our equity position after five years (all figures rounded to the highest one-thousand):

	House #1	House #2	House #3	House #4	House #5
Value	$97,000	$88,000	$80,000	$73,000	$66,000
Loans	46,000	46,000	47,000	47,000	47,000
Equity	51,000	42,000	33,000	26,000	19,000

How do you make the money? Do you sell? No. You refinance. And you attempt to find the highest possible loan on your properties. Help yourself to do just that. Paint the trim on the houses, maintain the yard, or consider new carpeting or draperies. You might even paint the interior throughout the entire house. Do as much as possible with as little money as possible. Your aim is to get the highest appraisal possible for your invested cosmetic dollar.

Then do your homework—be prepared to convince the appraiser that the value of the home is worth twice what it was five years ago. If you are able to obtain a new loan of 75 percent of the value of the appraisal, you should be able to refinance your first property for at least $75,000.

If your existing loan is $46,000, your net proceeds from the new loan will be $29,000, less loan fees, which may be as high as $2,000. So you should be able to keep at least $27,000 of the new loan, a figure that represents the equity that belongs to you and, as such, is not taxable. You will not have to report this income to the government as long as you don't sell the property (one good reason not to sell!).

Can you now rent the property for enough to pay the mortgage payment? A mortgage payment on a $60,000 mortgage at 13 percent interest for 30 years would amount to $820.75 plus taxes and insurance—perhaps as much as $1,000 a month total. Sound impossible? Remember, you're looking at rents five years down the road; they're bound to be considerably higher.

Still uncomfortable? Hold out $2,000 from your refinance profits. That will give $166 a month to apply toward the mortgage payment. You'll still have $25,000 left over to spend as you want to, and it's tax free. Kick off your shoes and pursue a full-time real estate investment hobby. Do this with one house each year. Refinance in January, and you're set for the year.

If you want to retire with an even higher income—insurance against inflation—buy two houses a year. Then, at the end of five years, start refinancing two houses a year. It's twice the work, but it will be twice the income. And you'll still have plenty of time for your new hobbies and lifestyle.

And once you have completed one full cycle of five refinanced homes, you can start all over again with the same cycle . . . *ad infinitum.*[1]

"Wealth depends on diligence."
—Hegel

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[1] I would like to thank Jack Miller and John Schaub for sharing their basic idea for the five-year retirement plan in their nationwide seminar entitled "Making It Big on Little Deals."

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The Nothing Down Real Estate Glossary: A Dialogue

Appendix

BY RICHARD J. ALLEN, Ph.D.

The Nothing Down Real Estate Glossary: A Dialogue

BY RICHARD J. ALLEN, Ph.D.

Welcome to the circle of Robert G. Allen Graduates! We thought you would enjoy reading the following dialogue as preparation or review for your investment activities. With a little practice, you'll find that creative finance terminology will become second nature to you—perhaps it already is! At the end of the dialogue you will find an alphabetized listing of the numbered entries printed in bold type in the text. Have fun! We look forward to having you as a participant in the ACRE Investment Program.

Meet Doug: Doug is a professional—bright, progressive, competent at his job. But he is new to real estate and a bit frightened by the welter of new vocabulary items used in buying and selling property. He needs a little coaching.

Meet Mark: Mark is an investor who knows from experience how to transact deals using creative financing. The vocabulary is second-nature to him by now. Still, he hasn't forgotten how tricky it was at the beginning to distinguish between puzzling things like a wrap-around mortgage, a second deed of trust, and a quit-claim deed. Let's listen to their conversation. Whether your name is Doug, or Jim, or Judy, perhaps this dialogue will help demystify real estate for you.

Doug: This real estate world is a bit baffling to me. Mark, I wonder if I am capable of learning the "script"?

Mark: Like every other human activity, Doug, the world of real estate investments has its own rules and setting. It's a dramatic setting—a stage with many roles and actors. There are really only two villains: fear and ignorance. The hero is the creative person who invests judiciously and progresses towards financial independence. The play is a tragedy if the main player lacks initiative and gets eaten alive by inflation or fails to take advantage of opportunities. The play is a romantic farce if the main character wastes his time eating pie in the sky and dreaming of lost treasures that he'll never see. The only script that makes sense is the one where the hero takes charge of his affairs, plans carefully, sets specific goals, masters the "Nothing Down" creative financing system, and puts it into effect. He doesn't wait to buy real estate, he buys real estate and waits.

Doug: There seems to be a huge supporting cast to this production. How am I going to sort them all out?

Mark: [Laughs] It's not as complex as you might think. Basically we're talking about a **buyer** and a **seller.** Of course, legal documents tend to use stuffy terms. Even so, all you have to do is keep your "-ees" and your "-ors" straight. The **vendor**[1] is a person selling something to the **vendee**[2] (or buyer). Sometimes they talk about the **grantor**[3],the person who transfers interest in a piece of property to the **grantee**[4] (or recipient). There are other parallels. In the rental market, for example, the **lessor**[5] (landlord) gives to the **lessee**[6] (tenant) the right to occupy a rental space. You see, the "-ors" have something

to offer (remember the "o" in "offer" and relate it to "-or"). The "-ees" have something to get (remember the "e" in "get" and relate it to "-ee").

Doug: That reminds me. I could never keep mortgagor and mortgagee straight.

Mark: It's easy. The **mortgagor**[7] (borrower) has something to offer—he offers a mortgage or trust deed (i.e., a secured I.O.U.) to the bank in order to obtain a loan. The **mortgagee**[8] (bank) has something to get—that's the mortgage or trust deed setting forth the provisions according to which the loan is to be repaid.

Doug: What's all this about a don't wanter?

Mark: The don't wanter is one of the main characters in the play! A **don't wanter**[9] is a person who is willing to sell his or her property flexibly—i.e., by giving you either *your* price or *your* terms (sometimes even both). The **terms**[10] refer, of course, to the amount of down payment, the size and frequency of the repayment amounts, interest rate, and so on. A true don't wanter is anxious to help you acquire his property. Perhaps only 5 percent of the sellers are true don't wanters. So we have to know how to locate them. That's an important part of the Nothing Down seminar.

Doug: How about the other professionals out there?

Mark: People involved in the sale of real estate have various titles. The **real estate agent**[11] (or **broker**[12]) is licensed in the state to negotiate a real estate transaction for another party for compensation. The **Realtor**[13] (a title, capitalized) is an agent or broker who is an active member of a local real estate organization affiliated with the National Association of Realtors, a professional association holding to a prescribed code of professional ethics. A **real estate salesman (salesperson)**[14] is licensed to transact real estate business but not by himself; he or she has to work under the direction of a broker. The broker, under the law, is the one who has the agent relationship with the person who seeks professional services.

Doug: Who is going to help me with all the documentation of real estate transactions?

Mark: That is the **title company officer**,[15] one of the most important professionals available to you. He serves as a neutral third party drawing up all the legal paperwork needed to transact business in real estate. The title company is equipped to carry out thorough examinations of the public records concerning a property and confirm its ownership, find out whether there are any encumbrances or liens against it, and any other facts that might affect its sale. The title company issues a **policy of title insurance**[16] guaranteeing compensation to the holder of the policy if any defects or problems with the title should show up later. The title company officer also frequently serves as the **escrow agent**[17] who holds and disposes of documents or funds according to the instruction agreed upon by the buyer and seller.

Other important professionals include the **appraiser**[18], who is trained to give an estimate or opinion about the value of the property in question. If the appraiser has the title **Member, Appraisal Institute (MAI)**[19], he or she holds the highest title or designation given by the American Institute of Real Estate Appraisers. Besides the appraiser, you may often need the services of a competent **real estate attorney**[20] to advise you on legal aspects of real estate, as well as a competent **accountant**[21] to handle the financial records, advise you on taxes, etc. In some areas of the United States and in Canada, for example, it is customary that attorneys (lawyers) perform many of the functions of the title company officer outlined above. You might also be using a professional **property manager**[22] to help you with the management of your portfolio.

Doug: It's a relief to know that I'll have a team to work with in putting all of this together. Could you give me some help with the world of real estate finance and ownership?

Mark: Sure. Basically you'll be dealing with "hard money lenders" and "soft money lenders." The former are the people whose business it is to lend money under very strict conditions of qualifying and repayment. Here we are referring to the **commercial savings banks**[23] (usually specializing in short-term loans) and the **savings and loan associations**[24] (up until recently specializing almost exclusively in long-term mortgage loans for residential real estate). There are also the **finance companies**[25] who mainly deal in second mortgage loans (usually at a very high rate of interest and for shorter repayment periods of five to 10 years or less). The "soft money lenders" are the people who lend without such strict requirements of qualifying and with more flexible repayment terms. Here we are thinking of the seller himself, who will frequently finance the sale of his property on a contract. **Partners**[26] you might be dealing with also belong to the soft money camp.

Doug: How about the specific terms having to do with ownership and borrowing money?

Mark: The most basic term of ownership is the word **deed**[27], which is the written document that is signed and acknowledged by the maker and serves to transfer ownership (i.e., the **title**[28]) of property from one person to another. There are refinements to that, of course. A **warranty deed**[29] is one in which the seller or grantor guarantees (warrants) that good title is being conveyed, whereas a **quit-claim deed**[30] simply transfers whatever title or right the seller has in the property at that moment and contains no warranty about the general quality of the title being conveyed. You'll see how the quit-claim deed can be used to protect you when you sell a property: you'll have the buyer execute one in your name and leave it with the escrow agent (title company officer) who will be instructed by buyer and seller to give it to you in the event the buyer defaults. That way you have security and protection.

Doug: How about the vocabulary of financing? I know what a mortgage does, but I would be hard pressed to define it.

Mark: The word **mortgage**[31] comes from the French and means essentially a "pledge until death." That is a rather solemn kind of I.O.U., isn't it? In reality, the documentation is not complicated. Basically you have two papers: one is the promissory note (I.O.U.) setting forth the terms of repayment of the loan. A second paper serves as the security document and says in essence that if you fail to perform according to your promise, the lender has the right to take over the **collateral**[32], in this case the property you have pledged as security for the debt. Usually the collateral is the specific property that is being purchased with the funds being borrowed. That's what happens when you buy your own home. For example, you go to the bank or S&L and say, "If you'll give me the money to buy this home with, I'll turn around and pledge it as collateral to secure the debt I have incurred in order to buy it in the first place."

Doug: What is the difference between a mortgage and a deed of trust? Don't they serve the same purpose?

Mark: You are correct, Doug. Keep this in mind as I explain the difference—for loans secured by real property, there are always two basic documents involved: a note (I.O.U.) covering the borrowed funds, plus a security document pledging the real property as a back-up to the loan. In some areas the security arrangement is based on a **mortgage**[33]; in other areas it is based on a **deed of trust**[34]. Here's how they differ. The mortgage arrangement

involves two parties (borrower and lender), while the trust deed involves three: the borrower (**trustor**[35]) and lender (**beneficiary**[36]), plus a third party called a **trustee**[37]. Title of the collateral property is conveyed in trust to the trustee with the condition that the trustee is to reconvey the title to the borrower upon satisfaction of the note (in this case called a **trust note**[38]).

Doug: What happens if the borrower defaults on the loan?

Mark: In the case of the mortgage, the lender will take legal action by proceeding with the **foreclosure**[39] process and the sale of the collateral property to satisfy the debt. In the case of the trust deed, the trustee already has statutory power (by statute of the area involved) to take steps to sell the collateral property to satisfy the debt. Since the foreclosure process for a mortgage is a judicial process—that is, it has to go before the courts, with court cases, court dates, and the like—it takes longer than a trust deed foreclosure. In some areas a mortgage foreclosure takes as long as 13 months, while a trust deed foreclosure takes only three to four months.

Doug: What if there is no bank or savings and loan association involved and the owner himself or herself serves as the lender?

Mark: That happens frequently, particularly in times of tight money. There are two basic approaches to seller financing. One involves what is called a **contract of sale**[40] or sometimes a **contract for deed**[41] or a **land contract**[42]. I think you understand what I mean by contract: that is a written agreement between buyer and seller containing the price and terms, a valid legal description of the property, and all other stipulations agreed to. In the case of such a contract (contract of sale, contract for deed, or land contract), the deed (hence title) does not actually pass to the buyer until the conditions of the contract are satisfied.

Doug: It sounds like what happens with an auto loan. You don't get title until the last payment is made.

Mark: Exactly. It works the same way when you buy real estate on a contract of sale. Meanwhile, the buyer gets all the benefits of property ownership, including appreciation, tax advantages, etc. Even though he doesn't have title until the conditions of the contract are met, he still has what is called **equitable title**[43]. Equitable title means that he benefits from (owns) any increase in his equity even if he doesn't yet have the deed.

Doug: What documents are involved in a contract arrangement?

Mark: There are three to keep in mind: the **contract**[44] itself, a **warranty deed**[45] which the seller executes in favor of the buyer, and a **quit-claim deed**[46] which the buyer executes in favor of the seller. The two deeds are held in escrow by the title company or other escrow agent involved. The buyer gets the warranty deed after he has satisfied the conditions of the contract. If the buyer defaults, the escrow agent is instructed to release the quit-claim deed to the seller who then recovers his property with a minimum of difficulty. Do you get how it works?

Doug: It's getting clearer to me. I am certainly glad that the title company officer or lawyer can see to it that all the documents are prepared correctly. What is the second approach to seller financing?

Mark: The other approach is referred to as a **wrap-around mortgage**[47] or in some areas as an **all-inclusive trust deed (A.I.T.D.)**[48]. Let's suppose the property has a loan against it. The owner's **equity**[49], then, is the difference between the **fair market value**[50] of the property and the amount of this indebtedness.

Doug: Just a minute. What do you mean by "fair market value"?

Mark: **Fair market value**[51] is the sales price a willing buyer and a willing seller agree upon when both are reasonably informed as to all the pertinent facts and neither is under any compulsion in the transaction. Of course, when the owner is a don't wanter, he might be willing to **discount**[52] his equity and the actual sales price will be below fair market value.

Doug: Clear enough. Go on.

Mark: Well, as I was saying, suppose there is already a loan against the property you want to buy. If you negotiate a wrap-around mortgage or an all-inclusive trust deed with the seller, you agree to sign a note that covers not only the balance of the seller's equity (after the down payment—if any) but also the amount of the existing loan against the property.

Doug: Why would the seller agree to do that?

Mark: Well, suppose the existing mortgage or deed of trust was costing the owner 9 percent interest, and you agree to an 11 percent figure for the "wrap" or A.I.T.D. On the amount of the existing mortgage or deed of trust (sometimes called the **underlying mortgage**[53] or **underlying deed of trust**[54]), the owner then picks up a 2 percent spread on money that isn't even his. Of course, he gets the full 11 percent on his equity above the original loan.

Doug: Not bad! Does title actually transfer in such an arrangement?

Mark: Yes, the buyer actually receives a deed and title transfers. And that is what has stirred up a bit of controversy the last few years. If the underlying mortgage or deed of trust was set up fairly recently, let's say within the last seven or eight years, it probably contains a **due-on-sale clause**[55], sometimes referred to as an **alienation clause**[56] or a **non-assumption clause**[57]. Such a clause states that the lender has the option of calling the entire balance of the loan due should the property be sold and title transferred to another owner. Thus it is possible, especially in the case of a wrap-around mortgage or an A.I.T.D., that the lender could call the existing loan all due and payable upon sale of the property.

Doug: What are the implications?

Mark: It would mean that the bank would want to have the new buyer **assume**[58] the existing loan, that is, take over the primary responsibility for repaying it, go through the normal process of qualifying, and probably pay an **assumption fee**[59] and a higher interest rate. The controversy arises when you come back to the issue of whether the bank actually has the right to exercise the due-on-sale clause, especially in cases where its interest is not jeopardized by the sale and transfer of the title. This issue is currently being litigated in the courts across the United States. The most famous of such cases is the **Wellingkamp Decision**[60] in California (1978) which stated that state-chartered savings and loan associations do *not* have the right to accelerate the loans in such instances. Naturally the federally-chartered S&Ls felt they were exempt, so the controversy continued to rage.

Doug: Wouldn't it be safer to assume the existing mortgage or deed of trust in the first place and make arrangements to pay off the seller's equity in a mutually agreeable way?

Mark: It depends on how you stand on the issue, whether you are willing to pay the assumption fee and higher interest rate and what the legal patterns are in your area. Always seek competent legal advice in such matters. Of course, if the existing mortgage or deed of trust is one that is insured (guaranteed) by the **Federal Housing Administration (F.H.A.)**[61] (in Canada, the Central Mortgage and Housing Administration — CMHA) or the **Veterans**

Administration (V.A.)[62], it is always assumable as is. There is never any problem assuming an F.H.A. or V.A. loan—no qualifying at all, and you have to pay only a small fee, around $50. The original borrower, of course, had to qualify for such a loan, but the person **assuming**[63] the loan does not have to qualify. It is the **conventional loan**[64] (i.e., non-F.H.A. or non-V.A.) with a non-assumption clause that has been so much in the center of controversy. It is only this latter type that causes concerns in the case of the wrap-around mortgage or A.I.T.D.

Doug: But doesn't the contract of sale method also involve properties that might have existing loans against them?

Mark: Yes, but you will remember that in the contract approach, title does not actually pass until the conditions of the contract are satisfied. For this reason, some buyers turn to the contract method where necessary, rather than the wrap-around mortgage or A.I.T.D. (where title is actually transferred). They are acting on the theory that the contract approach does not violate the provisions of a non-assumption clause in the underlying mortgage or deed of trust. The precedent for this line of reasoning is the **Lassen-Tucker Decision**[65] in California (1976), which seems to have become the basis for legal opinion in such cases in a number of other states. Of course, competent legal advice in your own area is essential, especially since the U.S. Supreme Court decision of June 28, 1982, upholding the right of federally chartered savings and loans institutions to exercise the due-on-sale provision.

Doug: I suppose that things can get fairly complicated if the same piece of property serves as collateral for different loans at the same time.

Mark: Well, it's really less complex than it sounds. That's where the **Office of the County Recorder**[66] (in Canada, the Land Titles office) comes in. While this office might have slightly different names in different locations, the function is the same—to "**record**"[67] mortgages, deeds, liens, and other important documents affecting a title of real property. The process of recording makes real estate transactions a part of the general public record, thus protecting the persons involved. When you set about to buy a piece of property, you will arrange for a title company or lawyer to conduct a **title search**[68] of the public records to make sure you have all the facts concerning the property in question.

Doug: Is that where the designation first, second, third mortgage, etc., comes in?

Mark: Right. This designation refers to the order in which mortgages or deeds of trust are recorded in the Office of the County Recorder. A **second mortgage**[69] or **second deed of trust**[70] is one that happens to be recorded later in time than the **first mortgage**[71] or **first deed of trust**[72]. In a foreclosure procedure, the proceeds from the sale will go to pay off the loans in the order in which they were recorded.

Doug: Is there any limit to the number of **liens**[73] that can be placed on a property?

Mark: There is no magic in the number of such liens. The critical factor is the **security**[74] involved. Let's say a property has a fair market value of $100,000, with a first mortgage of $60,000. The remaining equity of $40,000 is theoretically available as security for additional loans. There might be a second for $20,000, and third for $5,000, and so on, until the property is totally encumbered (100 percent financed).

Doug: You say "theoretically available."

Mark: Banks usually loan only up to 80 percent of the value of the property. Sellers, on the other hand, or private individuals, might be induced to accept notes

covering the entire value of a piece of property. That's why it is frequently more advantageous to work with private parties.

Doug: What if the property in question serves as security for loans totalling more than its fair market value?

Mark: We say then that the property is **over-financed**[75]. One must be cautious in such cases not to cross the threshold of legal propriety. One must be cautious to avoid offering real property in a fraudulent way as collateral for a loan. Always seek legal advice in such matters.

Doug: Could you sketch out the general contours of the acquisitions process?

Mark: Certainly. After you have located a flexible seller (don't wanter) and conducted one or more fact-finding sessions, you will want to complete your analysis of the property. Your major concerns will be location, condition, and financing. For properties larger than four units, the APOD is useful in financial analysis.

Doug: APOD?

Mark: Yes, the **Annual Property Operating Data**[76] form. It's a standard form that summarizes the expenses and facilitates calculating the **net operating income**[77] of a property (gross scheduled income less all of your operating expenses). Using the net operating income and the value of the property, you can calculate the **capitalization rate**[78] for the property.

Doug: Sounds a bit far-out to me.

Mark: Not really. The cap rate, as a percentage, is simply the net operating income divided by the value × 100. For example, if the N.O.I. for a given five-unit property is $8,000, and the value is $100,000, then the cap rate is

$$\frac{8{,}000}{100{,}000} \times 100 = 8\%$$

It's easy.

Doug: Now that I've got it, what do I do with it?

Mark: It's a comparison index. If properties in your area are showing cap rates of 7, 8, or 9 percent, then this 8 percent property might look pretty good to you. It's in the financial "ballpark." On the other hand, if the cap rate for a property is 4 percent in the same area, you might not be too thrilled with it. Either the seller is asking too much for the property, or there is a serious problem with the expenses, forcing the N.O.I. to be too small. In any case it is a red flag for you and almost certainly indicates a **negative cash flow**[79] situation when you go to make the payments on the loan.

Doug: That's what you refer to as an "**alligator**."[80]

Mark: Right. Any time you have to add money from your own pocket to take care of property, you've got an alligator. Of course, there are small alligators and large alligators. The bigger they are the more likely they are to eat you. Sometimes a careless investor will wake up and find that he's got a whole hungry zoo!

Doug: How do you avoid alligators and zoos?

Mark: That's where **creative financing**[81] comes in. After you have decided that a seller is flexible and his property is desirable, it's up to you to find the combination of creative (alternative) financing techniques that will enable you both to win. You solve his problem, and he solves yours. That's what we call **the win/win philosophy**[82]. The idea is to find a mutually agreeable way to buy the property for little or no money down out of your own pocket, with

the arrangement structured so that you avoid negative cash flows and also balloon payments that are too oppressive.

Doug: By **balloon payment**[83] you mean a repayment schedule where a large sum comes due somewhere down the line.

Mark: Exactly. You might make regular monthly payments for a period of time, say five years, and have the balance due in one balloon sum at the end of that period. In some cases, this might be a good way to go, but one can get carried away with it, particularly if the balloon payment is short term. One thing is for sure, such short-term balloon payments make the time slip by quickly!

Doug: What are some of the creative finance techniques you would recommend?

Mark: That's the subject of a whole session in itself. There are dozens of such techniques that might be applied in a given situation. That's the core of the Robert Allen Nothing Down Seminar. It's the most comprehensive creative finance seminar available.

Doug: Let's talk about the actual buying process. What is the first document that I will have to know about to buy property?

Mark: Because almost all transactions start with an agreement or offer to buy, the first document is an **earnest money agreement**[84] or **offer to purchase**[85]. This agreement states that a person is ready, willing, and able to buy. There are blank spaces provided for the terms of the transaction—provisions for price, interest rates, monthly payments, and any other conditions the buyer wishes to include. The seller then has the right to accept the offer "as is," reject it, or modify the terms. If he accepts the offer, he signs it, and the paperwork moves on to closing. If he rejects the offer, the deal is off. The buyer may submit another offer. If the seller modifies the agreement, he makes the changes or adds an addendum and sends it back to the buyer. In effect he is now making an offer to the buyer. This type of offer/counter-offer could continue through several changes. Once they both agree, the agreement is signed and then moves on to closing.

Also, most people now use standard (pre-printed) forms which cover the whole range of possible terms. These forms are designed for filling in the blanks. If the wording is not exactly what you want, feel free to adjust it with the help of a competent professional. This wording will have to stand the test of time because it lays the foundation for the terms that will be on subsequent documents. It's important to make sure that it's just what you want.

Doug: Is an **addendum**[86] something that is added to the offer to purchase?

Mark: Yes, usually on a separate sheet of paper. Reference needs to be made to the original document that it will be added to and more specifically to the paragraph or term on the original document that it will affect.

Doug: You mentioned **closing**[87]. Isn't the deal finished when both the buyer and seller agree to the terms?

Mark: Even though the purchase offer dictates what will now take place, the deal is not closed. Closing means that the proper papers are drawn up, signed, and recorded. If you are asked by an **escrow company**[88] to come in for a closing, it means that everything is ready. Once completed, title to the property transfers or an interest shows against the title as in the case of a real estate contract.

Doug: Is that all that an escrow company does?

Mark: Drawing up the papers is just part of it. As said earlier, the escrow company also orders a **title report**[89] and later a **title policy (policy of title insurance)**[90]. This lets you see whether or not the property is free and clear or whether it is

encumbered by other liens. It states whether the seller has the right to transfer title. It would be a good idea to request copies of the actual documents that stand against the title to the property. Especially if you're assuming those loans.

The escrow company also balances the books. They get the exact figures on the balances of the loans. They figure out the taxes and insurance, etc., and prorate it to the day of the closing (or other agreed date) so you'll only pay exactly what you owe.

Escrow companies also hold documents or money while waiting for other stipulated conditions to be met. It's advisable to get a good escrow officer on your team of experts. In Canada and some parts of the U.S., as we said earlier, the work of escrowing (title work) is done by lawyers specializing in real estate.

Doug: What is the difference between a **title report**[91] and a **policy of title insurance**[92]?

Mark: A title report is a current reading of the title status of a property. It shows all liens and encumbrances against a property and even any judgments or restrictions against the people or corporations who have an interest in the property. It will also show the current status of the property taxes. This report is also called an **abstract of title**[93].

One step up from a report is a **policy of title insurance**[94]. This approach is popular in the U.S. A Title Insurance Company researches the chain of title and everything else concerning the property (including verifying the legal description and any easements), and once they're certain everything is in good standing, they will issue a title insurance policy to the buyer insuring him against problems which might arise in the future for reasons not then apparent. This is also called a **certificate of title**[95].

Doug: So once I know that the seller has good title, the deal can proceed to closing?

Mark: That's right. If all is okay, the seller has a **marketable title**[96], meaning that he can sell or transfer his interest in the property.

Doug: It seems that the legal description appears on every document. Why can't we just use the street address?

Mark: Street addresses are not specific enough in that they don't refer to the actual size or boundaries of the property. Originally a plat map was drawn, and the legal description referred to that actual map. The legal description will be a **lot and block number**[97] (then city, county, and state), be computed by **metes and bounds**[98] (technical measurements) or by **government survey**[99]. The reason these are used is to avoid confusion and problems. If continually used in every transaction concerning a property (and used without changes), a good standard is set, and boundary and easement problems will be lessened.

Doug: It seems like the **chain of title**[100] is really important.

Mark: It is. The chain of title shows the different owners (or lien holders) of a property. It shows what instruments (deeds, mortgages, etc.) were used to transfer title through the property's history. We've previously talked about the different deeds and documents; now it's fun to see how a property has gotten where it is.

Doug: You mentioned that the escrow company or lawyer figures out the **closing costs**[101]. What are they, and who pays them?

Mark: Every area has a different set of closing costs. The common ones are the fees required to buy title insurance and pay for the escrow company's or lawyer's services. The buyer's charges for insurance, taxes, etc., are not actually closing costs, but they are figured on the same paper. Some areas charge a tax

(excise) on every property each time it's sold. There could also be revenue stamps to purchase. All of these fees are usually a small portion of the selling price, and most of them are divided between the buyer and seller. Your escrow company or lawyer can give you a good estimation of what they will be.

Doug: You said that the earnest money was a down payment. Can you explain further?

Mark: Accompanying the agreement is usually an amount of money or at least a promise to pay. This may be called a **deposit**[102], but whatever it's called, its purpose is to show the buyer's earnestness. If the deal goes through, this amount becomes part of the down payment or purchase price. If the deal is terminated, this money is retained or returned to the party not at fault.

Doug: Is there always a **down payment**[103]?

Mark: Most properties today are purchased with some sort of financing (either by the seller, a bank, or someone else). The down payment is the amount of money (or whatever satisfies the seller) between the sales price and the amount being financed. Down payment is frequently shortened to "down."

Now that we've covered all the basic terminology of creative financing, you should be ready for the Nothing Down Seminar.

Doug: I'm on my way! There's no stopping me now!

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— *Control Without Ownership.* Lease options. Four tapes and workbook. RETAIL $175.00 ACRE PRICE $157.50

— *How to Make the Ultimate Purchase Offer.* Clauses and techniques. Six tapes and workbook. RETAIL $139.00 ACRE PRICE $119.00

— *How to Get Start-Up Funds.* Tape and workbook. RETAIL $24.95 ACRE PRICE $19.95

— *How to Write a Firm But Fair Lease/Rental Agreement.* Tape and workbook. RETAIL $24.95 ACRE PRICE $19.95

— *Complete Real Estate Investor's Training Portfolio.* Includes all of the above items by Mr. Drummond, plus *How to Get Started in Real Estate Investing* (five tapes and workbook, $139 value), and a one-year subscription to *Phil Drummond's Investor Alert* newsletter ($36 value), packaged in an attractive attaché case ($40 value). RETAIL $578.90 ACRE PRICE $295.00

Dykes, James M.

— *Real Estate Bargains.* Includes *How to Find Real Estate Bargains,* six tapes; *How to Create Real Estate Bargains,* twelve tapes; and *Computer Analysis.* RETAIL $275.00 ACRE PRICE $225.00

Epley, Richard

— *Real Estate Survival Course.* Six tapes. RETAIL $195.00 ACRE PRICE $175.00

— *Junk Apartments to Cash Flow Machine.* Eight tapes. RETAIL $245.00 ACRE PRICE $225.00

— *Combination Offer.* All of the above items by Mr. Epley. RETAIL $440.00 ACRE PRICE $295.00

Fox, Claire R.

— *Syndicating Single-Family Homes: How to Form Group Investment Partnerships Using Other People's Money.* RETAIL $17.95 ACRE PRICE $16.00

Garrison, Marc

— *Retire with Real Estate.* A comprehensive guide to achieving financial freedom through real estate investing. RETAIL $31.00 ACRE PRICE $29.00

— *Real Estate Greenbook.* A complete real estate encyclopedia and reference guide. RETAIL $26.95 ACRE PRICE $25.00

— *The Financial Freedom Tape Set.* Two tapes: *Getting Started* and *Tools for Success in the '80s.* RETAIL $29.95 ACRE PRICE $25.00

— *Property Analysis System.* Finding, recognizing, and buying good deals in real estate. Two tapes, workbook, and forms. RETAIL $175.00 ACRE PRICE $139.00

— *The "Pro-Pak" Combination Offer.* All of the above items by Mr. Garrison. RETAIL $262.90 ACRE PRICE $189.00

— *The Real Estate Investors' Guide: How to Get Started.* Eight tapes and workbook. RETAIL $175.00 ACRE PRICE $126.00

— *The "Pro-Pak" Combination Offer.* The above combination offer plus *Investors' Guide.* RETAIL $437.90 ACRE PRICE $288.00

Gibson, Don

— *Cash at the Close: Real Estate Tools and Techniques.* Eight tapes, workbook, and contract and forms package. RETAIL $275.00 ACRE PRICE $225.00

— *Starting Over Again in Real Estate.* Four tapes. RETAIL $69.95 ACRE PRICE $49.95

— *Fortunes in Foreclosures.* Four tapes. RETAIL $69.95 ACRE PRICE $49.95

— *Combination Offer.* All of the above items by Mr. Gibson. RETAIL $414.90 ACRE PRICE $225.00

Glubetich, David

— *How to Grow a Money Tree: Earn 20 to 30 Percent and More by Investing in Safe, Hi-Yield Second Mortgages and Trust Deeds.* RETAIL $9.95 ACRE PRICE $8.95

— *Double Your Money in Real Estate Every Two Years.* How to turn inflation to your advantage. RETAIL $14.95 ACRE PRICE $13.45

— *The Monopoly Game: The "How-To" Book of Making Big Money with Rental Homes.* Buying and managing the single-family rental home. RETAIL $9.95 ACRE PRICE $8.95

Hall, Sam F.

— *Positive Solutions to Negative Cash Flows.* Dealing with balloon notes, lease options, shared appreciation, discounted mortgages, refinancing, seasonal demand properties, and others. RETAIL $14.95 ACRE PRICE $13.00

— *Positive Solutions to Negative Cash Flows Tape Package.* Companion to the book. RETAIL $24.95 ACRE PRICE $20.00

— *Combination Offer.* Book and tapes by Mr. Hall. RETAIL $39.90 ACRE PRICE $30.00

Koon, Nick

— *Getting Started Building Your Real Estate Investment Career.* Six tapes and workbook. RETAIL $169.00 ACRE PRICE $149.00

— *Buying Smart Systems to Build Your Cash Flow.* Six tapes and workbook. RETAIL $169.00 ACRE PRICE $149.00

— *Hard-Nose Landlording.* Six tapes and workbook. RETAIL $169.00 ACRE PRICE $149.00

— *Combination Offer.* Includes the above three items by Mr. Koon. RETAIL $507.00 ACRE PRICE $298.00

— *Becoming a Millionaire Buying Single-Family Homes.* Workbook. RETAIL $39.50 ACRE PRICE $24.00

— *Building a Zero Tax Bracket.* One tape. RETAIL $14.95 ACRE PRICE $12.00

— *Nick Koon's Famous All-Day Millionaire Seminar.* RETAIL $169.00 ACRE PRICE $125.00

— *Combination Offer.* Includes the above combination offer plus the next three items. RETAIL $730.45 ACRE PRICE $395.00

— *Getting Started—My Story.* One tape. RETAIL $14.95 ACRE PRICE $12.00

— *Will You Make It in Real Estate?* One tape. RETAIL $14.95 ACRE PRICE $12.00

— *Rules for Screening Tenants.* One tape. RETAIL $19.00 ACRE PRICE $15.00

Land, Joe

— *Paper: The Ultimate Tool for the Real Estate Investor.* Purchasing real estate using discounted mortgages, trust deeds, corporate bonds, etc. Eight tapes and workbook.
RETAIL $165.00 ACRE PRICE $148.50

— *Tax Strategies for the Real Estate Investor.* Eight tapes and workbook.
RETAIL $165.00 ACRE PRICE $148.50

— *Real Estate Tax Update.* Monthly newsletter; one-year subscription.
RETAIL $48.00 ACRE PRICE $43.20

— *Combination Offer.* Includes all of the above items by Mr. Land.
RETAIL $378.00 ACRE PRICE $275.00

Milin, Mike and Irene

— *Landlording Made Easy.* Six tapes and workbook. RETAIL $130.00 ACRE PRICE $119.00

— *Cash Flow, Cash Flow, Cash Flow.* Eight tapes and 213-page workbook.
RETAIL $249.00 ACRE PRICE $195.00

— *Money-Making Clauses That Get Results.* Two tapes and workbook.
RETAIL $75.00 ACRE PRICE $69.00

— *Pennies on the Dollar.* RETAIL $69.00 ACRE PRICE $59.00

— *Real Estate Investor Analysis.* Newsletter; one-year subscription and hotline.
RETAIL $165.00 ACRE PRICE $150.00

— Options and Government Loans tape series. RETAIL $149.00 ACRE PRICE $99.00

— *Combination Offer.* Includes all of the above items by Mr. and Mrs. Milin.
RETAIL $837.00 ACRE PRICE $319.00

Mitton, Jay

— *Keeping It! A Tax Program for the Eighties.* Workbook with sample trusts and estate plans.
RETAIL $195.00 ACRE PRICE $175.00

— *Keeping It! Tape Package.* Four tapes, companion to the workbook.
RETAIL $65.00 ACRE PRICE $57.95

— *Combination Offer.* The above workbook and tapes by Mr. Mitton.
RETAIL $260.00 ACRE PRICE $229.95

Morris, Hal

— *Crisis Real Estate Investing.* Low-risk guide for protecting assets and avoiding disaster.
RETAIL $19.95 ACRE PRICE $17.65

— *How to Stop Foreclosure.* How to save your home and property.
RETAIL $14.95 ACRE PRICE $13.45

— *Foreclosure Systems.* Eight tapes, workbook, and bank/savings and loan computer printout.
RETAIL $295.00 ACRE PRICE $225.00

— *Equity Sharing: An Answer for the '80s.* Six tapes and five contracts.
RETAIL $350.00 ACRE PRICE $295.00

— *Combination Offer.* Includes all of the above items by Mr. Morris, plus a nine-tape album, *Money-Making Ideas* ($73.95 value). RETAIL $753.85 ACRE PRICE $495.00

Murdock, Clint

— *The Bucks Start Here: How to Win With Your Banker.* RETAIL $14.95 ACRE PRICE $12.95

— *A Comprehensive Guide to Financing Options for Real Estate.* Expandable loose-leaf format. Learn about loan sources for financing single and multiple residences, etc.
RETAIL $125.00 ACRE PRICE $95.00

— *Bank Lines of Credit: How to Get Them, How to Use Them, and How to Grow with Them.* Includes two complete sample loan request packages. RETAIL $24.95 ACRE PRICE $22.00

Napier, Jimmy

— *Invest in Debt.* Investing in discounted mortgages. RETAIL $13.95 ACRE PRICE $12.00

— *Combination Offer.* Includes *Invest in Debt* described above, plus *Money Maker: 2-Day Home Study Course* (eight tapes), *Money Maker Report* newsletter (18-month subscription), *Live at Caesar's Palace: Guest Appearance with Jack Miller* (eight tapes), and *Negotiation* (six tapes).
RETAIL $447.85 ACRE PRICE $300.00

Nickerson, William

— *How I Turned $1,000 Into Five Million in Real Estate.* Fixing up investment property to build equity. RETAIL $18.95 ACRE PRICE $17.00

Phillips, Wayne

— *How to Get Government Loans.* Finding and using low-interest loans for qualified investment properties. RETAIL $75.00 ACRE PRICE $67.50

Prigal, Ken

— *The Winning Offer.* Six tapes and comprehensive manual. RETAIL $150.00 ACRE PRICE $125.00

— *Profits with Partners.* Book and four tapes. RETAIL $150.00 ACRE PRICE $125.00

— *Combination Offer.* Includes the above items by Mr. Prigal, plus one bonus tape and two *Impact* Reports: *The ABCs of Selling Property Part I* and *Part II.* RETAIL $345.00 ACRE PRICE $225.00

Robinson, Leigh

— *Landlording.* One of the best books available on property management. RETAIL $15.00 ACRE PRICE $13.50

Rotola, Al

— *The Trustee Game System.* A complete turn-key business operating system. Includes the marketing and procedures. RETAIL $349.00 ACRE PRICE $295.00

— *Fortunes in Foreclosures* Package. Includes *Megatactics Volume I: Fortunes in Foreclosures* (six tapes and workbook), and *Megatactics Volume II: Borrowing Big Money—Fast* (six tapes and workbook). RETAIL $330.00 ACRE PRICE $288.00

— *Megatactics Package.* Includes the above package, plus *Megatactics Volume III: The Seminar Tactic* (six tapes and workbook). RETAIL $495.00 ACRE PRICE $390.00

Santucci, Danny

— *It's Your Money.* Eight tapes and workbook. RETAIL $160.00 ACRE PRICE $139.00

— *Keep the IRS Out of Your Pocket.* Eight tapes and workbook. RETAIL $145.00 ACRE PRICE $124.00

— *Concepts and Mechanics of Exchanges.* Eight tapes and book. RETAIL $195.00 ACRE PRICE $175.00

— *Tax Planning for Closely-Held Businesses.* Six tapes and workbook. RETAIL $150.00 ACRE PRICE $130.00

— *Combination Offer.* Includes the four above items by Mr. Santucci. RETAIL $650.00 ACRE PRICE $450.00

— *Bonus Package.* Includes the above combination offer, plus *Impact of the 1984 Federal Tax Act* (four tapes and text, $95 value), *Partnership Taxation* (text, $85 value), and *Special Allocations: Transfer and Sale of Tax Benefits* (text, $35 value). RETAIL $865.00 ACRE PRICE $495.00

Schaub, John

— *Investing in Houses: How to Creatively Acquire and Manage Single-Family Houses for Your Investment Portfolio.* Six tapes and workbook. RETAIL $125.00 ACRE PRICE $112.50

— *Investing in Paper: How to Locate, Negotiate For, and Purchase Discounted Paper.* Six tapes and workbook. RETAIL $125.00 ACRE PRICE $112.50

— *Combination Offer.* Includes the above items by Mr. Schaub, plus a one-year subscription to *Making It Big on Little Deals: Update* newsletter (quarterly, $36 value). RETAIL $286.00 ACRE PRICE $225.00

Smith, Dave

— *The Time Value of Money.* Understanding the principles involved in financial transactions; using the HP-12C Calculator. Eight tapes and workbook. RETAIL $195.00 ACRE PRICE $145.00

— *HP-12C Calculator.* Available only with the above package by Mr. Smith. RETAIL $120.00 ACRE PRICE $90.00

Southard, Jim

— *Real Estate Wealth-Seeker's Guide.* Eight tapes and workbook. RETAIL $159.00 ACRE PRICE $129.00

Steele, Robert

— *Creative Real Estate: Problem-Solving Formulas.* RETAIL $35.00 ACRE PRICE $31.50

— *Creative Real Estate Tapes.* Ten tapes. RETAIL $199.00 ACRE PRICE $164.95

— *Fifteen Ways to Buy, Sell, and Exchange Real Estate Without Using Cash.* RETAIL $22.00 ACRE PRICE $19.80

— *Fifty Ways to Acquire Real Estate.* RETAIL $25.00 ACRE PRICE $22.50

— *An Extra House as an Investment.* RETAIL $19.00 ACRE PRICE $17.00

— *The Real Estate Exchange Market and How It Operates.*
RETAIL $25.00 ACRE PRICE $22.50

— *Mortgage Investments: Principles and Methods.* RETAIL $25.00 ACRE PRICE $22.50

Tauscher, Don

— *Borrowing Money Successfully.* Developing banking relationships— how to bank when others cannot. Twelve tapes and workbook. RETAIL $245.00 ACRE PRICE $190.00

— *Paper Magic.* The creative use of paper formulas to acquire investment real estate. Four tapes and booklet. RETAIL $85.00 ACRE PRICE $75.00

— *The Bank Book.* Guide to banks: banking basics, evaluating your bank or savings and loan, and getting the most out of your bank. RETAIL $15.00 ACRE PRICE $13.50

— *Combination Offer.* Includes the above items by Mr. Tauscher.
RETAIL $345.00 ACRE PRICE $265.00

Thurston, Wright J.

— *Diamonds in the Rough: Making Money in Multiple Units.* Six tapes and workbook.
RETAIL $195.00 ACRE PRICE $149.95

— *Making It Happen: How to be Rich.* Four tapes and workbook.
RETAIL $150.00 ACRE PRICE $125.00

— *Sixty Strategies for Successful Investing.* Two tapes and booklet.
RETAIL $75.00 ACRE PRICE $50.00

— *The "Wright Stuff" Combination Offer.* All of the above items by Mr. Thurston.
RETAIL $420.00 ACRE PRICE $249.95

— *Property Management Magic: Fair-But-Firm Landlording Techniques.* Four tapes, contracts, and forms. RETAIL $195.00 ACRE PRICE $149.95

Wayner, Stephen

— *Money-Making Tools.* Creative methods to buy real estate, including wraparounds, equity participation, trusts, etc. Six tapes and workbook. RETAIL $199.00 ACRE PRICE $159.00

— *I'm on Your Side.* Over 150 items (includes checklist) that belong in a real estate contract, plus Real Estate Analysis Sheet. Six tapes and workbook.
RETAIL $199.00 ACRE PRICE $159.00

— *Wayner's Legal Forms.* RETAIL $50.00 ACRE PRICE $45.00

— *Stephen Wayner's Legal Package.* Includes all of the above items by Mr. Wayner.
RETAIL $488.00 ACRE PRICE $299.00

Whitney, Russ

— *Home Study Course.* Includes *Overcoming the Hurdles and Pitfalls of Real Estate Investing; Rehabs: Basics and Realities* (six tapes and workbook: *Offers & Contracts*); *Salesmanship: The Winner's Edge in Real Estate Investing* (six tapes); *Financing, Locating, and Analyzing Real Estate: Overcoming the Hurdles and Pitfalls* (six tapes and workbook); and *Real Estate Forms Book.* RETAIL $590.00 ACRE PRICE $375.00

Zick, Barney

— *How to Make Your Real Estate Fortune.* Six tapes and workbook.
RETAIL $165.00 ACRE PRICE $99.00

— *The Midas Touch.* Six tapes and workbook. RETAIL $195.00 ACRE PRICE $145.00

— *How to Buy Right.* Six tapes and workbook. RETAIL $195.00 ACRE PRICE $145.00

— *"The Impatient Investor" Combination Offer.* Includes the three single items directly above, plus a six-month subscription to *Zick's Real Estate Financing and Mortgage Report* newsletter ($40 value). RETAIL $595.00 ACRE PRICE $295.00

— *How to Become a Paper Millionaire.* Six tapes and workbook.
RETAIL $195.00 ACRE PRICE $145.00

— *Equity Sharing, Small Partnerships, and Options* (workbook).
RETAIL $49.00 ACRE PRICE $39.00

— *Equity Sharing and Partnership Agreements.* Fourteen actual documents.
RETAIL $165.00 ACRE PRICE $99.00

— *Special Opportunity Series Combination Offer.* Includes the three single items directly above, plus *S.A.M.: How to Buy a House You Can't Afford, Using Shared Appreciation Mortgages* ($49 value). RETAIL $458.00 ACRE PRICE $395.00

— *"The Daddy Warbucks."* Includes the *Impatient Investor* combination offer and the *Special Opportunity Series* combination offer, plus discounts on a seminar for two people ($590 value). RETAIL $1,643.00 ACRE PRICE $395.00

FORMS AND INVESTOR AIDS

— *Consumer Guide to Mortgage Payments.* Financial Publishing Company.
RETAIL $5.95 ACRE PRICE $5.25

— *Creative Real Estate Forms* by Robert Steele. RETAIL $25.00 ACRE PRICE $22.50

— *Earnest Money Receipt and Offer to Purchase Form.* The Allen Group, Inc. Developed by Richard J. Allen. Package of 30 four-part carbonless forms.
RETAIL $10.00 ACRE PRICE $9.00

— *Financial I Calculator.* Full-function amortizing calculator. Easy to use.
RETAIL $33.50 ACRE PRICE $30.00

— *Leasehold Document Forms* by Robert Steele. RETAIL $25.00 ACRE PRICE $22.50

— *Legal Forms* by Wade B. Cook. Sample contracts, forms, and agreements.
RETAIL $22.95 ACRE PRICE $19.00

— *Professional Planner: The Forced-Focus System for Time Management* by Wm. Rolf Kerr.
RETAIL $69.95 ACRE PRICE $59.95

— *Realty Bluebook* by Robert DeHeer. A daily reference tool for use in every phase of real estate.
RETAIL $17.00 ACRE PRICE $15.25

— *Real Estate Dictionary.* Financial Publishing Company.
RETAIL $3.95 ACRE PRICE $3.55

— *Record-Keeping System* by Wade B. Cook. RETAIL $19.95 ACRE PRICE $17.00

— *Screening Sellers by Phone* by Sam F. Hall. Questions designed to glean information necessary to analyze potential investment property. Includes 50 analysis forms.
RETAIL $5.00 ACRE PRICE $4.50

— *Do-It-Yourself Legal Forms* by Stephen Wayner.
RETAIL $50.00 ACRE PRICE $45.00

— *Who's Who in Creative Real Estate* by William R. Broadbent.
RETAIL $25.00 ACRE PRICE $22.50

The American Congress on Real Estate
A Membership Organization of The Allen Group, Inc.
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Provo, Utah 84603-9000
(801) 373-8000

Confidential ACRE™ Case Study Form

Dear Colleague:

Congratulations on your recent "Nothing Down" creative real estate purchase. Your success would be an inspiration to the other members of the ACRE network who are anxious to improve their investment skills.

Would you please take a few minutes to share the details of your purchase with us? If your case study is featured in our materials (*The Real Estate Advisor,* special reports, case books like *How to Write a Nothing Down Offer,* etc.), we would like to say *thanks* by sending you a $50.00 voucher redeemable against any of the ACRE books, newsletters, tape products, seminars, workshops, or conferences.

By submitting this case study, you automatically qualify for the ACRE Letter of Commendation, which will be sent to you by return mail from the office of the National ACRE Merit Programs.

In addition, you may also qualify for the "Wise-ACRE" Award and receive a handsome certificate if the purchase outlined in this case study satisfies one or both of these requirements: (1) even or positive cash flow with no balloons; (2) purchase price at least 30% below market. The "Wise-ACRE" Award confirms that you have obtained your "acres" wisely!

☐ Check here if you believe your case study qualifies for the "Wise-ACRE" Award of the National ACRE Merit Programs.

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I would be happy to share my comments and the details of my purchase with you for use in ACRE literature. I understand that you will use fictitious names in any featured case study unless I specifically request that my real name be used."

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Signature Date

☐ Initial box if you wish your *own* name to be used in any featured case study.

_____
Occupation

_____
Name (please print)

_____
Address

_____
City State Zip

(_____) _____ (_____) _____
Home phone Work phone

Here's How I Did It:

1. How I found out about the property _____
2. Type of property (SFH, duplex, etc.) _____
3. Located in (city/state) _____; any unique features _____
   _____
4. Rent situation of property when I found it _____
   _____
5. Seller's situation (why selling, his price and terms, special needs) _____
   _____
6. Most important questions I asked in the negotiation _____
   _____
7. What I learned from the seller that helped me structure my offer _____
   _____
8. Looking back, my secrets for effective negotiation were _____
   _____

9. My offer, together with any changes the seller wanted (show price, terms, down, interest, unique twists, etc., use stick-house sketch if necessary; please show underlying loans; please give interest rates, length of term, and monthly payments on loans):



10. How I came up with the down payment _____

_____

11. The closing (date, who drew up documents, any special problems, etc.) _____

_____

12. Outcomes (rent adjustments, cash flow situation, future plans with property, etc.)

_____

13. Special clauses or phrases I like to use in my offers or closing papers _____

_____

_____

(If at all possible, please send photocopy of offer and closing papers . . . strictly confidential! When considered for publication, preference is given to case studies with documentation.)

14. If I could go back, I would make the following changes _____

_____

_____

15. The most important advice I can give others is _____

_____

16. Other properties I have bought _____

_____

17. Any other thoughts on the Nothing Down and/or ACRE Programs in retrospect _____

_____

_____

_____

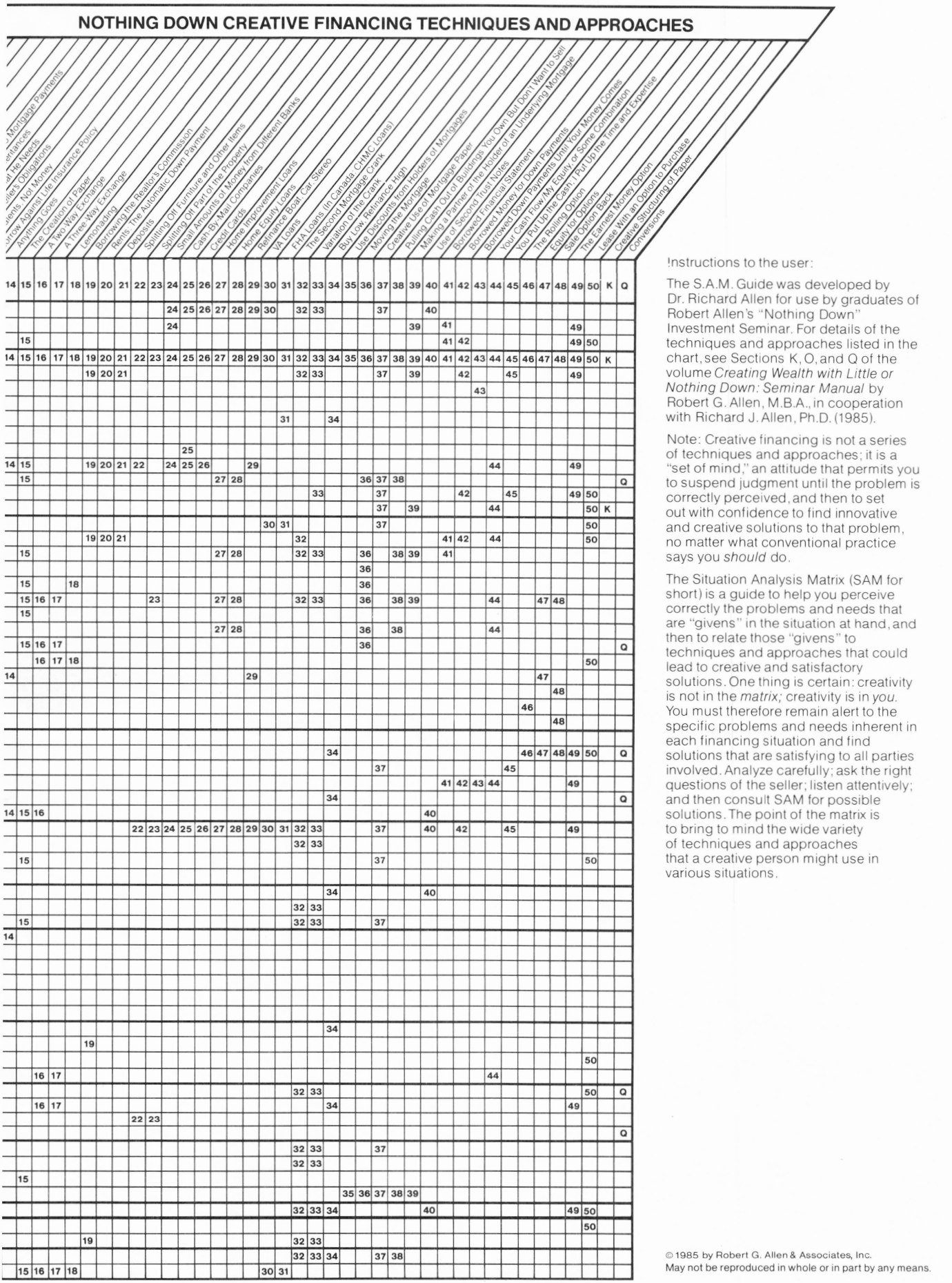
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sam Situation Analysis Matrix

A Guide for Relating the Details of Specific Investment Situations to Relevant Techniques in Robert G. Allen's "Nothing Down" System of Creative Financing in Real Estate

CATEGORIES		THE SITUATION AT HAND	1 The Ultimate Paper Out	2 The Blanket Mortgage	3 Life Insurance Policy	4 The Wrap-Around Mortgage	5 Raise the Price, Lower the Terms	6 The Balloon	7 Down Payment	8 High Monthly Down Payment	9 Defer the Down Payment	10 Your Own Savings	11 Supply the $	12 Assur
YOU AS THE BUYER	Your Credit Situation	You have good credit (or access to credit), but no cash right now.										10	11	
		You have poor credit.	1			4								
		You wish to avoid credit checks, qualifying, and closing costs.	1			4								
	Your Cash Situation	You wish to put down little or no money of your own.	1	2	3	4	5	6	7	8		10	11	12
		You have absolutely no money down.	1				5			8				
		You are short on cash now, but have money coming in later.						6		8				
		You have cash value in a life insurance policy.												
		You have cash or inheritances to invest.				4			7		9			
		You need a forced savings program as part of your investment plan.							7					
		You have a good cash flow, but no cash reserve for the down payment.							7					
		You have a short fall on the down payment and need a bit more to make it work.					5	6	7			10	11	12
		As a property owner, you wish to generate cash for down payments.												
		You have no property, but wish to generate cash for down payments.												
		You need to solve a negative cash flow problem.												
	Your Equity Situation	You need to buy a home to live in, but have little cash for a down payment.												
		You have no equity at all.	1			4	5	6					11	
		You have a weak financial statement.		2										
		You have property, but wish to increase its marketable equity quickly.												
		You have dead equities that you cannot seem to move or put to good use.		2										
		You have real estate equity that you can use in transactions.		2										
		You wish to make full use of your real estate equity, but don't want to sell, refinance, or take a second mortgage.												
		You wish to use your equities and are willing to refinance, but not to sell.												
		You would like to pyramid your assets into bigger properties.		2										
		You want to sell without incurring tax liabilities now.				4								
		You have equities in personal property (i.e., other than real estate) that you could put to good use.			3									
		You want to cash out some development land you own, but don't want to give up the future value of it.												
		You have development property that would be too expensive to acquire all at once.												
		You have development property that is going to be valuable in a few years, but you need to use the cash value in the meantime.												
	Your Other Resources	You have professional skills that the seller could use.												12
		You have an especially keen market sense.												
		You have time to invest in creative purchases, but no money.												
		You have a number of friends who have money or other investment strengths you lack.												
		You have fix-up skills (or access to them).					5	6						12
		You have second trust notes owed to you that you could apply.												
THE SELLER	Seller's Cash Needs	Seller needs cash down at closing.									9			
		Seller with low mortgage needs substantial part (but not all) of equity in cash.												
		Seller mostly interested in monthly payments.	1			4			7					
		Seller is not looking for a great deal of cash down, but wishes to improve his profit posture (e.g., higher interest rate).				4	5							
	Seller's Willingness to Compromise	Seller is willing to discount his equity.								9				
		Seller is willing to refinance his own property prior to sale.												
		Seller is willing to consider the use of second trust note in transaction.	1				5	6	7					
	Seller's Specific Needs and Concerns	Seller doesn't *need* cash, but insists on down payment as security.	1							8				
		Seller is highly-security conscious and suspicious of creative financing.		2	3									
		Seller has need of specific professional services that you could provide.												12
		Seller has need of debt relief.											11	
		Seller has specific personal purchase needs.										10		
		Seller is approaching retirement.	1			4								
	Seller's Needs in Regard to Selling	Seller must close quickly.	1			4								
		Seller would like to avoid closing costs.	1			4								
		Seller would like to avoid immediate tax consequence.	1			4								
		Seller doesn't want to give up investments altogether, but has trouble managing larger units or dealing with negative cash flows.												
THE PROPERTY	The Nature of the Property	Property lends itself to fix-up improvements.					5	6						12
		Property located in less promising neighborhood, but is still a good buy.					5							
		Property has furniture, equipment, extra land, etc., that you don't need.												
		Property has potential for conversion.												
	Mortgage Situation	Property is free and clear.								8				
		Property has low mortgage, high equity.												
		Property has VA or FHA mortgage (readily assumable, lends itself to contracts).	1			4	5							
		Property mortgaged by private lender(s).												
	Price	Property is under market, discounted.					5	6						
	Other Factors	Property rents are below market.												
		Property is listed with an agent.												
THE MARKET		When market is loose, consider especially the following:												
		When market is tight, consider especially the following:	1	2		4								



Instructions to the user:

The S.A.M. Guide was developed by Dr. Richard Allen for use by graduates of Robert Allen's "Nothing Down" Investment Seminar. For details of the techniques and approaches listed in the chart, see Sections K, O, and Q of the volume *Creating Wealth with Little or Nothing Down: Seminar Manual* by Robert G. Allen, M.B.A., in cooperation with Richard J. Allen, Ph.D. (1985).

Note: Creative financing is not a series of techniques and approaches; it is a "set of mind," an attitude that permits you to suspend judgment until the problem is correctly perceived, and then to set out with confidence to find innovative and creative solutions to that problem, no matter what conventional practice says you *should* do.

The Situation Analysis Matrix (SAM for short) is a guide to help you perceive correctly the problems and needs that are "givens" in the situation at hand, and then to relate those "givens" to techniques and approaches that could lead to creative and satisfactory solutions. One thing is certain: creativity is not in the *matrix;* creativity is in *you.* You must therefore remain alert to the specific problems and needs inherent in each financing situation and find solutions that are satisfying to all parties involved. Analyze carefully; ask the right questions of the seller; listen attentively; and then consult SAM for possible solutions. The point of the matrix is to bring to mind the wide variety of techniques and approaches that a creative person might use in various situations.

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