RACE FOR $50,000.00

GREGORY PINNEO

WWW.REACHRETURNS.COM

There we are. At the start line of the race. Each of us with our shoes tied tight. No money, no phone, no assets, no lines of credit, nothing except for what we know and how we think. The guns go off, and if only by instinct, we both start running…..but to where? What would you do? Where would you go? What is your strategy to win the race? First one back to the start line with 50K after tax cash wins the race. Ready or not……Bang! The race has started.

For some, working harder is the only instinct. To be sure, hard work is admirable. Work ethic is a lost virtue. With no where else to turn, this runner makes it their intention to put in more hours and save. If they are an average American, this plan would look something like this. If they could manage to save $500.00 a month they would have to earn at least $700.00 extra per month gross. This would mean working about 6 extra hours a week, or a little more than an additional hour each working day assuming their employer has work and wants to pay. If they were focused and diligent with this plan, they would have their 50K saved up in just about eight years. It would be hard to say what the actual buying power of the 50K will be at this time, but it would be there and they would cross the finish line working an additional 2400 hours give or take to get this done. Working harder is not always working smarter, but in deference to a known alternative, most go this route.

In the real estate game, there are a multitude of strategies that one could employ to win this race. The umbrella of real estate entrepreneurship is a wide one indeed, and under it are many specialties and ways to focus time and energy. Each racer is free to choose his or her own path.

Some may choose to "wholesale" properties. Another term for wholesaling is "assignment". Simply put, the entrepreneur is out finding excellent "deals". When they think they have a winner, they write the deal up, get it under contract, and then proceed to find a wholesale buyer to assign their purchase contract to for a fee. Usually the deal gets looked at by the wholesale buyer during some inspection contingency, feasibility study, or some other time buying contingency. If the wholesale buyer likes the deal, they agree to pay an agreed upon assignment fee to take over the contractual rights of the deal. An assignment fee varies widely, but in today's market most wholesale buyers are looking to buy in the lower end of the price / value spectrum. A typical assignment fee might be between 3K to 5K. If we used 4K as an average, this strategy would need to have about 18 deals found and assigned to net the 50K we need to win the race. To find 18 wholesale buyer worthy deals I would guess that the racer would need to look at about 200 to find the 18 that are worth doing. Understand that to look at this many birds takes a ton of time. This strategy also involves a lot of competition, as most wholesale / assigners work pre-foreclosure, foreclosure, and REO properties. I call these "adversity list" properties. The problem here is that every one of these buyers is working with the same lists. How many deals would you have to bid on in order to land the 18 you need to then hopefully assign them successfully to win the race? I cannot say an exact number, but what I do know is that to close 18 assignment deals is no easy task.

Another real estate racer might go the route of buying a property, fixing it up, and reselling it. Can we buy a property with none of our own money? Sure! Can we finance the rehab without using our own money? Sure! And can we put this on the market, get a buyer, and net our 50K after tax profit? Sure! It can be done. I have done it in three fold fashion just recently. However, we need to look at this and assess the risks and the likelihoods. If I were to work this deal backwards to net an after tax 50K, I would estimate that we would need gross sales profits around 80K. This would leave enough to pay our entire seller closing costs, and pay our short term capital gain. If we said our end price was $250K, we would need to be in this property all said and done no more than $170K. Backing this up, and figuring a cosmetic rehab of about 10K, we would need to buy this at about $150K to pay for the rehab and our carrying costs and buying closing costs. So, we would need to buy this property for $150K with an after repaired value of $250K, and we would need to be convinced that the $250K selling price is still at least 20% under market value to ensure a quick, all cash sale. Of course, negotiating the 150K to buy and the 20K to rehab and carry is also on our "to do" list. Perhaps the owner could finance the underlying, and we could get a short term investor loan for the rehab. It is unlikely that a new "first time" buyer, which is our market, would be able to cash us down to an assumption. It would cost them 100K down to assume our underlying, and if we offered to wrap the underlying, they would still need to give us at least 80K down to pay back our costs and tax obligations and give us the 50k cash we need to win the race.

The biggest challenge with this plan is not in the finding or the buying or even the funding, the biggest risk is in the selling part of the equation. Our home is on the market with a wave of competition.

The commission side of the business is always an option, but before you commit to this race strategy I think I would interview at least 20 brokers and see how they are doing in this market. Listing agents have product sitting everywhere. This does not lead to commissions being paid. Buyer's agents are super busy, but conventional financing is so crazy right now that only those who are working with superior buyers are taking deals to escrow and closing them. Many buyers' agents are going the route of the foreclosure market for their buyers, and again here they are frustrated with the mass of competition for any deal that is worthy. Before you go sign up and get your license, be sure this is the right race strategy for you. The average commission statistics would say that this race for 50K might turn into a marathon for you.

At the sound of the gun, there would be no hesitation in me. I would sprint to the blue collar, salt of the earth, neighborhood. Older, established, conservative and brimming with opportunity in this market. Once there, I would be looking specifically for a four plex. The four plex is the largest "single family" multiplex. If I ever sell, it brings not only investor buyers; it also brings owner occupant buyers and qualifies as a single family dwelling for loan purposes. I would be focusing on an older building, well kept, and simple in every way. Like a dog, the building usually looks a lot like the owner. Simple, well kept, conservative, nothing fancy. That is my kind of seller. Flashy, complicated people do not own 1958 two story walk up Tom Bodet leave the light on looking buildings. Simple, practical, conservative people own these types of buildings. This is the seller that I can have a discussion with. As much and maybe more than the building, I am seller hunting.

My 4 plex is very simple. 800 foot two bedroom one bath units. The rents for each are currently $500.00 a month. Rents have not been raised in five years. They used to be $490.00 a month. Tenants have been here forever. They each have a parking spot in the carport. The owner pays for water, sewer, and garbage. The tenants pay for their own electric. The current owner collects the rent, pays his taxes, insurance, utilities, and sets a bit aside for maintenance. Most of the gardening and fixing they do themselves. There is a small laundry room with a coin-op washer and dryer. It is 50cents to wash, and 50cents to dry. They empty the coin box about twice a year. What is left over each month after collecting the $2000. / month in rents and paying the bills is about $1300.00. The owner wants to retire, travel, and live in the warmer climate at least half the year. There days of being here and managing their 4 plex have come to an end. It is time to sell….but to who, and how?

I will be educating these folks on the benefits of an installment sale as it relates to the deferral of capital gain tax. The tax assessed value of their 4 plex is 330K. If they listed the building at 330K and got a full price offer they would net approximately 300K before tax. If they got cash and paid Uncle Sam capital gain with their zero basis, they would have about 255K to go and invest in something secure that would give them an income stream. What would they invest in? What would their income stream be? One thing for sure, they would need to really work to get better than 3% in this climate, and if this were a bank investment, only 100K of their 255K would be secure and insured.

My offer to them would be 315K. I would give them 15K down and the 300K on a note at 4.5% interest. Their interest only payment would be $1125.00 a month. I would borrow the 15K down short term at 12%. My payment on this loan secured by a second on the property would be $150. / month. I would raise rent to $595.00 / month. Once the rent raise kicked in, my gross monthly would be $2380. / month. I would take out 30% for expenses and this would leave me $1604. I would pay on my first and second and I would have $329. / month left over. This leverage able equity allows me to borrow. I would seek to borrow 65K and I would offer 7.5%. People with money in the bank, a CD, a bond, or a self directed IRA would be attracted to the security and return. With the 65K, I would use 15K to cash out the 12% second and place the 65K note in second. In that I have raised the rent by $380.00 a month, and did not add to my expenses, my value increase at a 6 cap. Is 76K . The new value of the building is at least 400K, supporting well a 300K first and a 65K second. When I pay on my first at $1125.00 and on my second at $406.00 this building still has a net positive per month of $73.00. I have 50K after tax cash in my pocket and I am on a sprint back to where we started this race.

I am not saying I am right, but I like my race strategy. It uses the momentum of our day and uses it to help put this deal together. Sellers are listening these days. They know it is not a good time to sell. They know lenders are all messed up. They are willing to hear proposals that will get them where they are going. Offering the seller 4.5% is a great return in light of the re-investment options, and in light of capital gain going up, it gives the seller even more incentive to think installment. Bringing in a 12% short term loan is easy. This loan is everywhere, and the final 65K second at 7.5% with a conservative income source of repayment and solid collateral is a much better investment option than most with money are currently experiencing. I have a good long term

hold, a positive cash flow, and I am back with 50K net in a matter of a few months with a single deal. Less deals means less things to go wrong. The difference between a glider and a helicopter.

Are you working hard? I think it is impossible to work hard with sustainability if you are not passionate about what you are doing.

Are you working smart? Is your strategy well thought out? Do you have the tools and the mindset to execute your strategy?

I would suggest that the winner of the race will always be the one who runs hard with passion, and the one who runs smart. This combination is hard to beat.