Quack, Quack, is it an Investor Deal or a Realtor's Lame Duck?

Don't Forget the BREIA Meeting tonight starting at 5:30 at the IGFA Fishing Hall of Fame in Dania!

I spoke at two realtors' conferences in the past couple of weeks. These realtors patiently listened as I droned on about how to make much more in commissions and fees than they are making currently on the same deals they are getting 6% on currently. In some cases they are getting as little as 1% after slicing and dicing their paltry commissions. In addition, I showed them 17 ways to do real estate transactions with little or no money, no credit and no risk. I don't know the exact figure but probably 90% of all realtors are closet investors and this group was no exception.

At the end of the meeting I was asked if I would review some deals they saw and possibly split the profits if I could get the deals to work. This is always a dilemma for me as I always want to help people, but our baseline of what a deal should be is vastly different than what the average investor or realtor understands. Realtors are used to evaluating deals to get commissions and thinking about retail, full-market value buyers. As investors we know we have to make a profit on every deal and thinking low is very wonderful, not ugly. These are mutually exclusive goals for the same properties.

I guess what aggravates realtors is to see investors buying properties and sometimes later the same day, selling them and making huge profits. Once a realtor "gets it" about how we search and find deals, he/she isn't all that interested in making a couple of percent commission on his/her transactions. But, there is a problem for them to get started and it is their baseline of what is a deal is generally way too high in terms of what they should pay for properties.

The best way to explain this is from an example just last week. A realtor from one of the two seminars sent me an email with a property for sale. It read, "I have a property that is listed at $135,000 and a seller who will take no less than $75,000, is it a deal?" I replied that it could be and to send me the info – address, pictures, etc. The address, pictures off the MLS and some info about the property followed shortly thereafter.

The pictures showed a nice property with all its appliances in perfect condition – obviously recently rehabbed by an investor. As I looked at the neighborhood on XIMA I saw that most homes were selling in the $35,000 to $55,000 range. In addition, I noticed that the seller had purchased the property just one month earlier for $55,000 and likely put $20,000 in a rehab and carrying costs – sounds a lot like the $75,000 above.

Without too much effort I could see that the investor wanted out and was probably willing to take a loss to do it! I am not the brainiest guy on the melon truck, but it was obvious that the seller/investor was a rehabber who paid too much for the property to begin with and was trying to get a cash buyer to take the "problem" off his hands, or I should say, "pass the hot potato on to another investor or retail buyer who didn't know any better." In short, this rehab deal may be a career stopper for the investor but a retail listing opportunity for a realtor.

The investor may have overlooked that the neighborhood would never support a $135,000 sale, but maybe he expected to bring in a buyer with a $70,000 cash down payment and get a small loan besides. Perhaps he didn't figure on a seasoning issue, ugly appraisal, or the inability of so many perspective homeowners to get loans. A couple of these surprises coupled with a hard money loan and renovation cost overruns can easily be a career-ending deal for a new investor. As is often happening recently to new rehabbers they are becoming unintentional landlords instead of rehabbers.

What about the realtor and the deal? A newbie might be initially seduced into thinking this was a deal. After all, it was listed for $135,000 (but not selling), it was in perfect rehabbed condition (but not selling) and the seller/investor took a $60,000 price cut (still not selling) but magnificently negotiated by the realtor. I forgot to mention that there could be serious code violations if the investor didn't pull permits and the property had been tagged by code enforcement.

Having said all that about the dangers of rehabbing in this market, I couldn't have planned it any better if I had tried because the local newspaper ran a front-page spread on how homes could now be bought for less than $50,000 in South Florida. I was very interested to see one story about a new investor who did a rehab on a house she bought for $47,000 and sold for $99,900. Sounds like every investor's dream, a $50,000 profit in real estate investing with a modest amount of capital (small to some, huge to others). Let's look at the reality of the transaction and a possible alternative that is much easier, quicker, and requires little or no money.

I have to assume certain costs, so be a little forgiving with me. I only rehabbed in South Florida for 25 years so I could be off-base on some of my estimates. The purchase price of $47,000 was closer to $50,000 even with the pro-rated tax credit at the closing and because of the long holding period. The investor could have asked for a re-assessment because of buying the property so late in the year and maybe she did. I got over an $800 refund on a similar priced property in the same neighborhood just last year, but likely no one told her that there is an exception to the filing period for year-end buyers.

The articles said the property was purchased last year and sold in March of this year, so that sounds like five months+ to me. If she used hard money, the cost was 1% per month or about $470/month x 5 months = $2,370 plus 2 or 3 points at the closing – I won't add any points in as she could have used her own money. The rehab was approximately $15,000 according to the article. The investor had to know exactly how much she had in the rehab and from the list of issues she had to repair, I believe it was much closer to $20,000+ than the $15,000 as expressed in the article.

If it was sold through a realtor then assume another $5,000 profit loss and if sold to an FHA buyer, the funding costs could have been another $5,000. With these figures in mind, let's add up the expected "profit" as I am guessing she made:
$99,900 – ($47,000 + $3,000 + $2,370 + $20,000 + $5,000 + $5,000) = $17,530 profit. There is nothing at all wrong when you take a profit in real estate investing. I could be wrong by as much as $10,000, and I am going to GUESS that she actually made a $25,000 profit for the sake of this example. Good job and she plans on doing 3 – 4 more in the next year according to the article. Based on the money she invested (assume she only funded the repair costs if she borrowed the purchase amount), she got a terrific return on her investment. I personally congratulate her.

On the flip side of the coin, two days before the newspaper article ran, a mentor student closed his first wholesale deal. His purchase price was $149,950 with a $1,000 escrow deposit which was his personal risk in the deal if he didn't close. However, we sold it to a cash buyer in two days and closed two weeks later. The sale price was $180,000 so he made a $25,000 profit after a $5,000 partnership fee to another investor. His total money in the deal, besides his $1,000 deposit was **ZERO ($0.00) DOLLARS**.

Oops, I forgot he paid our attorneys $350 to shadow the deal, which he was reimbursed as an expense and he got his $1,000 deposit back at closing. We closed by asking the buyer to use his funds to buy the property from the original seller and he agreed (in writing), so not even transactional funding was needed. **Market risk was ZERO, funds needed ZERO, time for the transaction to happen – SAME DAY (is that another "ZERO?").** No permits, no hassling with handy men, no anxious waiting for a buyer to appear as the months pass by, generally not much of a comparison with the rehabber above except one very important thing - **<u>the profit was the same</u>**.

Think about this, what if the rehabber above had wholesaled in between getting her deal and selling it? She probably wouldn't have needed much money to wholesale and with a modest profit of $12,000 a deal, she might have made more money by wholesaling for 5 months x $12,000 profit per month = $60,000 profit in the same time as her rehab. Can anyone do this kind of volume very easily? No, actually some students are doing a deal a week from our last mentoring program, but even more have not done a deal yet.

Unfortunately, some students will never do a deal despite the success all around them and all the help we can give them. Their comfort level is not so uncomfortable that they are willing to make the life changes that are necessary to achieve these goals. We all have fears and weaknesses and they can be handled or they can be crippling.

If you haven't done so already, ask yourself, "What's in my future?"

To your limitless success,

Dave Dinkel

P. S. I am publishing an article a day and you can see where to get them below – sign up, dig in and learn while you earn! I submit two articles a day to EzineArticles.com but they don't always get published daily. They won't publish some of my articles because they are "controversial" in the editor's mind. Obviously, he isn't a real estate investor; if he was or was going to invest he would have them on the front page! "Life isn't just fair, it's exactly as it should be" and when you get that, your life will change forever.

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