Sandwich Lease Options

Your Complete Guide to Buying & Selling on Lease Options eBook

Wendy Patton

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Introduction

Lease Options: Anyone Can Do It!

Fourteen-year-old John and his father attended a seminar I spoke at in Houston several years ago. During one of the segments of the presentation I usually teach my students how to call sellers directly out of the newspaper or from Craigslist. When I teach this part of the class I make live calls to sellers for the benefit of my students so that they can hear what I say to the seller and how I gather information to determine whether or not their home is a potential candidate for a lease option. On this day, however, I didn't even make any calls – we were simply talking about best techniques for calling leads.

The next day, while John was in school, he began circling the "For Rent" ads. After school he started making calls and followed my script – with no caller training – and he got a seller lead for a lease option who said "yes" they'd like to consider it. However, being only 14 and having no experience, he couldn't and didn't know how to enter into a legal contract. He went to his father and said, "What do I do?"

John ended up selling the lead to another investor in their local investment group for $500. He gave me a copy of his $500 check. Not bad for a fourteen-year-old kid and one to two hours of work. John immediately went on to develop a relationship with a local investor, and on his next deal (while still 14!) made 50 percent = $14,000 - of profit for his assistance in the deal. He has since done additional deals for much higher profits.

How and why can a fourteen year old kid do this and yet most adults would not? Is it fear of the seller saying no? Is it fear of the seller saying yes? Either way it is FEAR! We are afraid of failure. I believe we all have fear of failure and/or fear of success. At fourteen, he was not afraid of failure. Heck, he probably hadn't even been dumped by a girl yet ☺. He just applied what he learned and tried it. When you know what to say and when to say it, it makes it so much easier.

You are never too old or too young to start investing. If you can do the research and pick up the phone to make the calls, you are on your way. However, many of us stop before we even get started because of fear. We let that get in our way of success. We might have excuses of:

"I can't possibly do that."
"It's a young person's game."
"It's an older person's game."
"No one will say yes to me."
"I have no experience."
"I don't have a good voice."
"I don't have money."
"I don't have good credit."
Insert yours HERE…

All are negative talk and incorrect statements.

What's going to make you successful with lease options? *Taking the plunge*! One of my favorite sayings is: *Smart and Successful People Take Action Now and in the Present Moment.* You'll make some mistakes along the way, but so what? As long as you can get over the "I'm okay with myself if I make a mistake," then what's the worst thing that can happen?

John wasn't hampered by fear, and so was able to jump in, take the plunge and make things happen -- setting his financial future in motion. His example is by no means a huge amount of money, but nothing to sneeze at either. It is a fantastic amount for most people and extraordinary for a 14 year old. The money is not only important because John can now pay for college, but now John *has choices*. If he continues on his path in real estate investing, he will have the possibility of being independent and working for his own interests, unlike most of his friends. Choices are freedom!

For me, the most exciting facet of real estate investing is Future Financial Freedom - or as I call it - FX3. Everyone has different definitions of freedom. For some, it is financial; for others, it means having more control over their time. Let me have one of my BootCamp students explain this in their own words to you first:

Dear Wendy,

Our financial future has literally changed within the past couple of weeks by applying what my husband and I learned from your BootCamp. Even more importantly, what we've learned from your on-going, personalized support – you truly are the best! Keep in mind, my husband thought that I was crazy when I signed us up for your BootCamp and flew up from Florida to Michigan to hear you speak. It truly was the best thing we have ever done. Please share my personal testimonial with your classes. I'm a believer, this does work!

First off, I have to mention when we attended your seminar we had just completed a 1031 exchange, which gave us the great opportunity to start our investing career by buying 3 houses. Yes, it was so great having 3 houses sitting empty and one with a renter that lived off of us for free! This renter was so nice she gave a whole room to her pet rabbits to roam freely in after we had just re-habbed the house!!!

During the BootCamp my name was drawn to purchase a house on a lease option. Yes, I jumped for joy like I had just won a prize. The next day after the Coronas wore off I figured out what I had just committed to – a house that is a 1,000 miles away, where it actually snows, the pipes freeze, and they have things called basements! Yes, being from Florida this is just what I've always wanted - NOT!!! We were up for the challenge and Wendy made it so easy with her support along with the great contacts and help that we had from others who attended the boot camp. Not only did we get a great purchase price and terms with the owner, but today we have a pending contract for a lease option that will cash flow us

$600 a month and at the end of the 18-24 month term we will profit $107,400!!! Gosh, I guess that will cover the cost of the class – TRULY AMAZING!!!!

When we came home from Wendy's class we decided no more renters. We turned around booted the bad renter out, (and no we didn't keep the rabbits!) We sold all of our houses on lease options. So my 3 houses we had sitting empty, we now cash flow $700 monthly and we will profit within 18-24 months, $227,900!!!!!

Now comes the best part . . . I finally put Wendy's class to the test. I went out and found an owner that was willing to do a lease option with me. Every Realtor I spoke to, (and many investors as well), told me no one in their right mind will do a lease option with you in this market. The Florida market is way too hot. They are right. It is hot. Appreciation in some of our areas is anywhere from 34-40%. I got a gorgeous house that looks brand new on a lease option. I also got a killer deal on the rent at $950 a month – normal rent would be $1425! I did put $5,000 down which will come off the purchase price. They were asking $200,000 and it's worth $239,000, so I offered them $210,000. The terms are 14 months, enough time to refinance it if I have to. My new tenants bought it on an 18-month term. We will cash flow on a monthly basis $845.00 ($500 of that will be applied towards the purchase price) and we are selling it for $299,900 – that is a profit of $89,900. Amazing, is this for real??? I've since quit my job and I'm doing this full time. Thank you again Wendy for changing our lives!

D. and E. Larson

Why I Chose Real Estate

Deal making may just be in my blood. I've always loved a deal, and the day I realized real estate investing was that kind of game was the most important day of my life. My first house was a three-bedroom bungalow in a suburb of Detroit. I had just moved into town for a corporate job and there was no housing available—I lived in a hotel with all the other corporate recruits. My PITI (principal, interest, taxes and insurance) was $438. I rented two bedrooms to two friends from the hotel for $250 each. I had cash flow and I was living free! My $62 cash flow per month paid my credit card payment. I was 21 years old and I thought this was pretty cool! So I decided to do it again. I did that three more times that first year. I had no money or assets, but I did have credit cards (which I do NOT recommend using for real estate).

At the start of my real estate investing career, I was $20,000 in debt with student loans. In my mind, the worst thing that could have happened was that I would go bankrupt. However, I had good credit and was able to make my down payments on homes with credit cards. It wasn't long before I had a credit line of over $250,000 – and too many credit cards. Using credit cards should be the last resort for most investors as I lost a lot of profit by having huge revolving credit card debt – even though I faithfully made payments on all of them and somehow juggled them so that no payment ever slipped through the cracks! It was, however, an administrative nightmare. Still, I couldn't focus on that. I had to focus on what was the best that could happen. I could end up with FREEDOM and CHOICES!

When I started investing, I didn't know about lease options. I thought what I did was a zero down deal and something very creative. I didn't know of any gurus at the time that focused on buying on options, so I developed my own tools and systems to buy homes with little or no money down using the same techniques I was using to sell. I have since purchased almost every course available in the market on options, and learned extra tidbits from them all to add to how I do my business. I am the only national educator in the country that teaches people how to work with Realtors to find these types of zero down deals. Over the years I have fine-tuned the techniques that really work. I have completed hundreds and hundreds of lease option contracts.

I have bought and sold over 600 properties since becoming an investor in 1985. I have had as many as 175 properties in inventory at one time. My current and longer-term goal is to have 30 free and clear in my inventory. I would have been there already if the Michigan market hadn't tanked so bad in the last 5 years. I have invested in multiple states and continue to look for new opportunities throughout the country and internationally.

Wendy's Advice on When to Leave Your JOB
(Just Over Broke)

If you want to pursue real estate investing, in particular lease options, I don't advise you to quit your job and start with nothing. Instead, I offer this advice:

1. Start this business while you are still employed at your current job so you won't have to worry about receiving a paycheck while you learn the business.

2. Begin to build a second income that can eventually replace your primary income (your JOB).

Many people leave their jobs too early only to find out they must go back because they can't survive without the income. Don't make that mistake!

Whether you've left your job to pursue your own dreams of becoming a baker, a pilot, an artist or a Realtor® – we all have the same concerns and fears about starting out in a new business venture where we have to rely on our own efforts to make a payday. Even then, the first couple of years can be rough. It takes a while to "pay your dues" in any new skill – and learning real estate is a skill – but real estate not only has immediate profits through lease options, it can automatically provide investment income by the very nature of appreciation or equity buildup (to be discussed later in this book). Real estate builds a tangible future that can set you up for life if you have the passion and the drive to dig in and overcome the fears of trying something new.

I am so glad I pursued my dreams in real estate many years ago. When I left corporate America in the mid-1990's to pursue real estate full time, it was the best career move I have ever made! It has given me financial freedom. Do you want to be free? Real estate can give you Future Financial Freedom (FX3) too!

This book will share my secrets and strategies of Sandwich Lease Options with you. I suggest you try them all and decide what works best for your personal style and your specific area of the country. As you find your niche, you will perfect it. Real estate investing changed my life and it can change yours too. May lease options and zero down strategies change the way you think and help you live out your dreams so that you may have all the choices and freedom you desire!

Wendy Patton

CHAPTER 1

How Sandwich Lease Options Work to Get You to Future Financial Freedom (FX3)

What are Lease Options?

Lease Options are a way to purchase real estate, usually with very little or no money down, sometimes even with money back in the investor's pocket. Sound too good to be true? Well, it isn't. Can an investor end up with money in their pocket and not have to put 10 to 20 percent down to purchase real estate? Yes. These techniques are commonly used today by hugely successful investors. This book is going to show you how you can find sellers and homes you can purchase with little or no money down – truly the fastest way to Future Financial Freedom (FX3).

A lease option is a strategy that gives an investor the right to lease a home and also the right to purchase the home during or before the end of the lease period. An **option** is a contract that gives its purchaser the right to exercise a privilege. In the case of real estate investing, it gives the investor the right to purchase property during a contracted period of time. It is a technique that involves gaining *control* of a property, without the added burdens of ownership. All money made in real estate is made by *controlling* property. Owning property is the most obvious way to control it, but control is possible without ownership – and control is what makes the money. It was a dying John D. Rockefeller who told all of us his secret to achieving great wealth, "Control everything, own nothing." All of today's most successful real estate developers utilize options.

It is important to be aware that there are some risks involved with this technique, but I will cover these risks later on to help you minimize your exposure. The rewards that can come with lease options truly far outweigh the risks, so long as you keep aware of all that is involved. All real estate investing involves some level of risk. Lease options, because of how they are done, are truly the safest way to invest (in my opinion). Real estate investing is truly the quickest and best way to build lasting wealth. Many of the world's wealthiest people acquire much of their wealth through investing in real estate and also using options.

While sandwich lease options can build you tremendous wealth, they usually shouldn't be considered a short-term investing strategy. I define a short-term strategy as one in which the time that passes from the start of the transaction to completion (cashing out) is less than one year. A classic example of this would be a rehabbing project (fixing up a house and reselling it). The other side of the spectrum would be a longer-term strategy, such as buying a rental property and renting it over many years. I consider sandwich lease options to be in the center of that spectrum, usually requiring one to three years for the best payoff. However, you can always immediately sell the deal to another individual or investor for a profit; this is what is called in the business **wholesaling or cooperative lease options** (more on my website about these techniques). This can be done if you buy the property at a low enough price that you can turn a profit by selling the deal to another investor at a discounted price.

Visualize This Scenario

In every seminar I teach, I ask the students, "Who of you would be willing to purchase a home valued at $200,000 for $100,000." Of course all hands shoot up. Then I continue by asking if they would still be willing to purchase the same home if the price was $150,000. Most of the hands stay up. I proceed upwards with the price increasing the increments by $10,000 each time. I always watch with amazement as the hands slowly but surely drop. At the price of $180,000 almost all hands are down. The point I am trying to make to each of them is that most investors are not willing to pay this close to retail price for a home.

I then re-pose the question to them: "How many of you would be willing to pay $180,000 for a $200,000 house with no money down, with a 10-year time to pay the $180,000 to the seller at $1,000 per month? Oh, how about if we say all $1,000 of your payment each month gets applied to the price of $180,000? Now are you interested?" Now all their hands go back up. I ask, "Why, now, are you willing to pay $180,000 for that home that you wouldn't have a few minutes ago?" They respond in unison saying, "Because you added some attractive terms!" My response is always the same: "You didn't ask the terms before!"

Terms are parts of a lease option deal, such as price, amount down, length of time to pay, monthly payment, monthly credits, and other negotiated items with the seller, which will be discussed further and in more detail in later chapters. Many times even experienced real estate investors don't ask, "When does the seller need his cash?" They say "no" to a price before they ask when the seller needs his/her money. The previous example illustrates how most investors think -- they don't ask all of the right questions about the property before they make a decision. They look at the surface but they don't dig deeper for other possibilities.

Lease options provide a creative solution that can allow you to *negotiate terms* that can increase your profits and provide a great investment opportunity. Now you are able to pay a higher price on a home if you can get reasonable terms, and having this tool at your disposal allows you to open up many new possibilities and make money on deals that were before completely ruled out. It's all about terms!

When doing any lease option deal, it is one of my mottos that everyone must win or don't do the deal. There are 3 people involved: the seller, you the investor and the tenant/buyer. It must be a win/win/win; otherwise walk away.

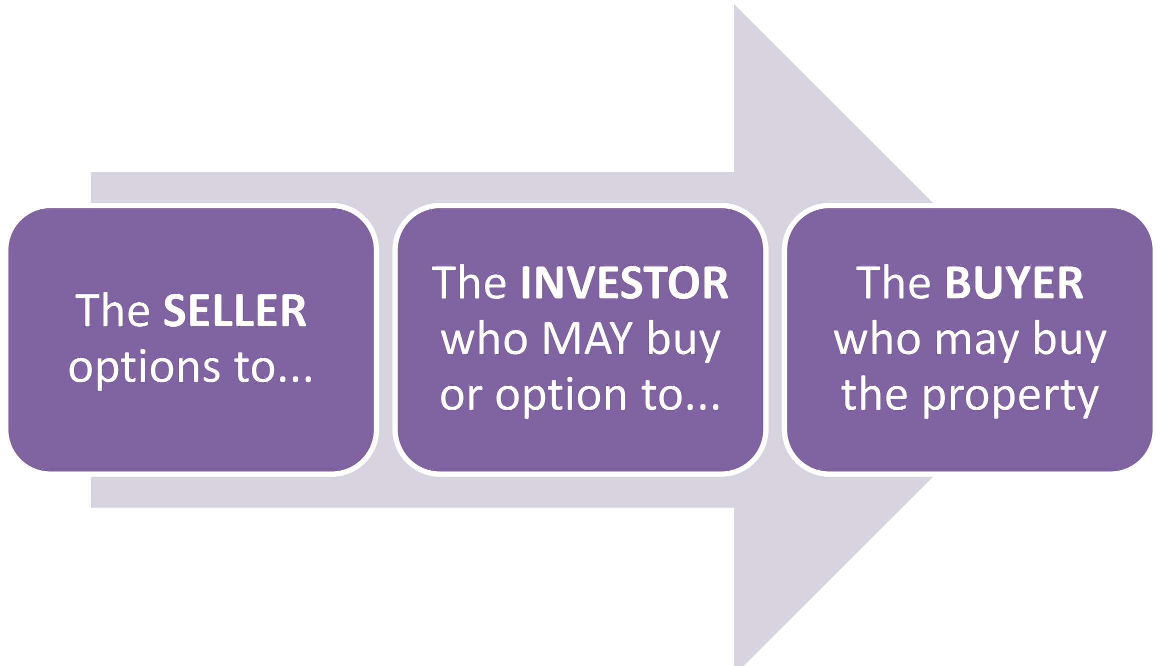
Wendy's Advise on Sandwich Lease Options

If it isn't a Win/Win/Win for the *Seller*, the *Investor*, and the *Tenant Buyer* then walk away from the deal. There are plenty of the deals out there where everyone can win.

Standard Lease Option Deals

My typical strategy is to lease option from a seller and then to lease option that home to a buyer.

How Lease Options Work

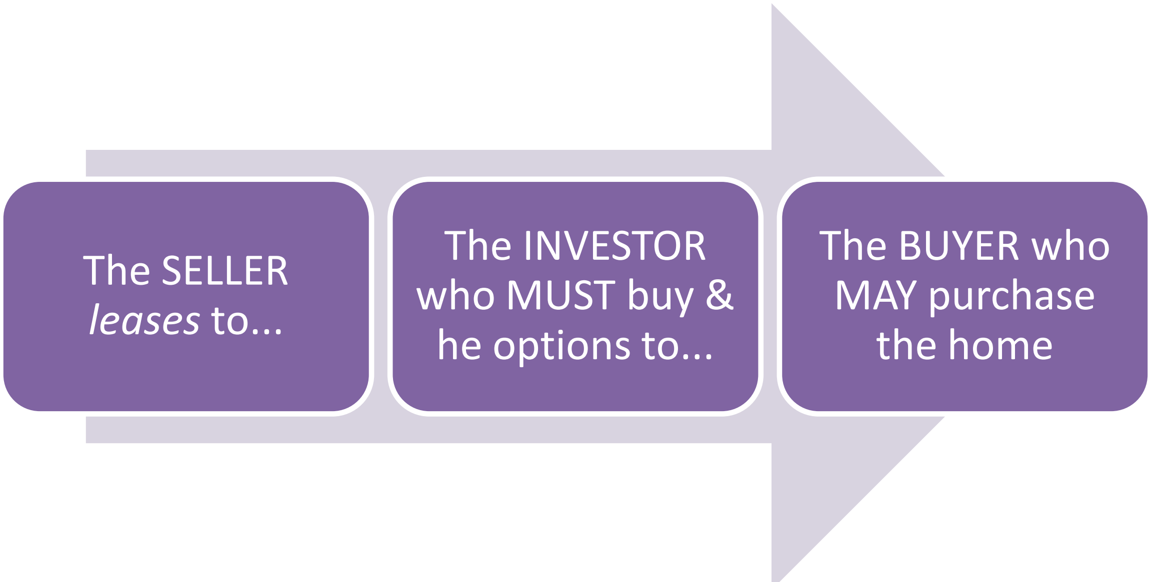


The above illustration depicts a **Sandwich Lease Option**. In a sandwich the meat is in the middle. The best part of a sandwich is the meat, and you (the investor) are in the middle of the transaction; your reward (the meat) is the difference between what you paid for the home and then what you sold it for. There are also ways to make this deal even better and more profitable, which will be discussed in later chapters.

A variation of a Sandwich Lease Option is the **Cooperative Lease Option**. In a Cooperative Lease Option (discussed on my website) the investor finds a seller and does a lease option with them, and then "flips" or assigns their contract to an end tenant buyer and keeps the option fee. They do not stay involved or in the middle.

One other possibility is a **Lease Purchase**. While a lease option gives the investor the right to purchase real estate, the lease purchase *guarantees* that he or she will purchase the property during a given time period. Therefore, use lease purchases with much caution.

How Lease Purchases Work



Lease Option Deal

Here's a great real-life example from my files of a lease option deal from start to finish – a true win/win/win:

The seller: Janet

Janet, a seller, answered an ad I had placed in a newspaper. I placed an ad that read:

> **Company looking for 3-4 homes in the area, on long term lease. Call 123-222-2222.**

Janet's home had been listed on the market for $189,000 with a Realtor and had recently expired. She saw my ad and decided to call. She's exactly the person I was looking for. She was *willing to sell* and also *willing to do a long-term lease*. Bingo! I still had to determine some other factors to make sure it would be a win/win/win.

Janet's most important area of concern was her price, and she was set at $185,000, and she was not going to budge on that portion of the deal. As soon as I knew that Janet was set on this one area of negotiation, I could work with the other areas of the terms for myself (see Chapter 3 on Negotiation). I would need to look at the rest of the terms to see if I could still make this a win/win for my side of the deal. These days I do not say no as quickly as I would have years ago; I look at the *entire* deal now, instead of getting caught up with a traditional style of price alone deal structuring.

Janet fixed her price, and so I had to look at monthly payments and the timeline available. By having all the facts I was able to analyze the entire deal, and thus make sure I would still obtain MY bottom line of profitability. At the time of this particular deal we were in a strong appreciating market – approximately 6-7% per year. So I figured that at $185,000, with 6%, that would be about $10,000 per year just in appreciation. I had really hoped to get the property for $175,000. Even with $10,000 in appreciation after the first year, I would only be where I had originally wanted to be in the first place! I did end up buying the house for $185,000, and put $4,000 of improvements into the property (just basic carpet and paint). I now had $189,000 into the property. Selling it for anything above $189,000 would be pure profit.

Janet was not in trouble financially but she was motivated to sell! She had a severe shoulder injury that was preventing her from doing the maintenance around the property. She made great money, and could have hired someone for the maintenance, but decided that with 20 plus surgeries under her belt and more to go, she just wanted some time outside of her large home and yard to deal with. She didn't need her money out of the property, but she did ask for $1,000 up front so she could go rent a lake front home in the area. The $1,000 I gave her for the option fee, plus the $4,000 for improvements, was a total of $5,000 out of my pocket for this home, which is less than 3 percent down. In the scheme of things this is a small amount down for this home.

The Buyer: Roberta

I knew Janet and I were going to come to terms and do the necessary paperwork on Sunday so I ran an ad on that same Sunday and I got a call from Roberta. I told Roberta that she could drive by the home but that she could not go in yet or on the property, because someone still lived there. Roberta didn't even know I didn't have the deal tied up – I just wanted her to drive by and see if she liked it.

Roberta had poor credit and *seven dogs*. Most landlords won't rent to someone with seven dogs, and most mortgage lenders won't do a mortgage for someone who has poor credit. With an inability to get a mortgage she is also unable to work conventionally with a Realtor®, so what is she going to do? No one will rent to her, and no one will give her a mortgage. This puts many people in a situation where they desperately need a solution. I am trying to help people with this type of situation. They want the American dream, yet they are unable to obtain it any other way.   *Lease options give people a second chance to improve their credit while working towards the purchase of the home they desire to own.*

If you're a landlord, all you get up front on any of your rentals is the security deposit, and that is just not enough cash to take on the risk of someone with poor credit and seven dogs. You can change this scenario by converting these people from tenants to tenant-buyers. Then, the risk that once was on you is shifted to the tenant-buyer - where you truly want it. With Roberta putting a lot of money down (option fees are not refundable), she was taking on the risk.

Let's look at how the deal transpired:

My Out of Pocket costs:

Option Fee to Seller (Janet)	-$5,000.00
Improvements	-$4,000.00
Option Fee from Tenant Buyer (Roberta)	+$10,000.00
Leftover in my pocket	+$5,000.00

I didn't even own this home and yet I had $5,000 in my pocket. Roberta is the one risking $10,000 with her option fee, as it is non-refundable. If she doesn't buy, she's walking away from a lot of money. She now has a lot of risk on her also with her $10,000 option fee.
Janet asked for $1,100 per month, and I in turn asked Roberta for $1,450 per month. That way I was able to pay Janet and still have a cash flow of $350 per month which would add to my profitability in the deal. In this case Janet had a lot of equity in the home, and I was able to leverage that equity to get her to accept the lower monthly payment of $1,100.

The option sale price I set for Roberta was $225,000. How did I get that figure? I put a 10 percent option premium on top of the retail price (to be discussed in a later chapter – Determining Profitability of Deals) plus I added an additional 6 to 7 percent appreciation rate at 18 months which was approximately another $20,000, I rounded it up a little to get to $225,000.

Now I understand that you may or may not have appreciation in your market at the time you're reading this book. It doesn't matter if you do or don't; you account for that in the beginning before you make your offer to purchase.

What was the property actually worth? Value is always determined on what a buyer is willing to pay. Roberta later had the house appraised at $267,000. Did I lose $42,000? I don't think so. After all, I did make about that much. Was Roberta happy with the appraisal? OF COURSE! Janet is happy because she got the price she wanted, and Roberta is happy because she's suddenly has an appraisal that gives her an additional $42,000 in equity that she can utilize if she wants. Janet won, Roberta won, and I won. I believe this demonstrates what a classic win/win/win deal is all about.

Here's my profit at closing: Not bad for not actually owning anything (except for 2 hours) – just controlling it!

Front end cash	$5,000
Back end sale	$31,000
Tax Pro-rations	$2,800
Cash flow x 14 months	$4,900
Total Profit	$43,700*

* It is not exactly $43,700. There are transfer fees in a few states, title insurance fees, and I give my buyers option credits each month when they pay their rent on time. The extra $2,800 on tax pro-rations was given as extra profit to me also (not available in most states - a bonus when both the buyer and the seller paid for property taxes at closing. Only one person needed to pay for property taxes. Therefore, the extra $2,800 is given to the investor in the middle of the sandwich lease option deal.

Wendy's Ethics Rule

Don't do lease options with potential buyers who have no way of ever being able to get a mortgage. That's just being greedy and taking advantage of someone. It is not fair to the buyer. If the buyer screws up – shame on them! If you screw them up – shame on you!

Financial Freedom – You can get there!

This examples show you how lease options can be very profitable. The previous example is a fairly simple version of the lease option technique, as there are many other creative ideas you can do to make them more profitable and more complex as you choose (covered in chapter 9). Remember, you may need several deals just to lay the groundwork for your future financial freedom. It doesn't happen with one deal, and it doesn't happen overnight. However, with persistency it truly can happen!

There are several "paydays" using these techniques:

1. **Upfront Option Fee** from your buyer
2. **Monthly Cash Flow:** the difference between what you pay a seller & what your buyer pays you
3. **The Backend:** the difference between what you owe on the home & what buyer owes you

While the option fee is non-refundable, don't get excited on your first deal by immediately going out and buying that big screen TV you've always wanted. What if something happens down the road in six months? In owning or controlling real estate there are things that come up that are completely unexpected: broken furnaces, leaking roofs, unpaid rents, etc. Plan ahead for those things and you will be safe. If you have held the option funds in reserve, you will be able to cover your expenses. That's just good business sense. Yes, the money is yours to keep, but be wise with it because you may need it. You might actually want to put it aside entirely for a "rainy investor's day" so that you will be prepared. Then after the deal closes, you can take another look at the money because not only will you have that initial option fee, now you'll have the backend from the closing. As you are getting started in this business or any other business, it is important to be conservative with your cash flow and money. I recommend you keep your spending very tight and conservative. Also, you may want to be prepared to buy the next property should a good deal be offered up to you. Unfortunately most of our country does not have good spending habits, and therefore these habits allow people to get into financial trouble. It is very important to be on a strict budget for this type of business. If this will be hard for you, then you may want to find some outside help to get you on a system, which can enable you to get this set up. I cannot stress enough; it can be a make or break for people!

Let's say you made $30,000 overall on the deal. Here's one positive way to use that money:

Reinvest. Reinvestment will continue to bring income, but you will also want to pyramid your income. For example: if your first property made $30,000 overall and you received $5,000 in an up front option fee, now you're going to want to look for 2-3 new properties, probably with the same profit ranges. You'll need money up front to pay your option fee to the seller, even though you will reimburse yourself later with the option fees from the buyer. Also, the properties may need repairs that will also need to come out of your pocket up front, so you need to have the funds available from the previous sale. During this time you will probably still be keeping your day job just to keep enough cash flowing in while you are building your new business. Reinvesting also doesn't just mean pouring money into new properties. It can also mean purchasing new office equipment, software or anything else you need to continue to build your business. Maybe it's time you trashed that clunker computer and got one that was made in the 21st century, install a 2nd phone line or get bookkeeping software. I cannot stress enough: be prepared for your future!

At this time my average deal is $40,000 in profit for a sandwich lease option. Lease options typically turn over every 18-24 months. Depending on what part of the country you reside in the profit range will vary from $20,000 – $120,000 (Midwest to Northern California). You decide how much you need to make, and then you will know how many homes you need to lease option. Not only can lease options set you up to live today, but they can set you up for *Future Financial Freedom* and retirement.   Just sit back and imagine…how would it feel to be completely debt free? Real estate is the vehicle that can allow you to achieve just that.

Wendy's Ethics Rule

Don't do lease purchases if you don't intend to follow through on the transaction. Do what you say you will do and when you say you will do it. Help keep real estate investing an honest profession.

CHAPTER 2

Success Stories of Sandwich Lease Options

The best part of doing a lease option deal is being able to witness the end results. Unless a deal is a win for each party, walk away from it. The seller must win, the investor in the middle must win, and the tenant-buyer must win. When all three can win in a transaction, there is nothing better! This chapter contains stories shared by different investors in different parts of the country. The sellers' and buyers' names have been changed, but the numbers and details reflect the specific transactions. These deals will inspire you and show you how you can also be successful and create unique solutions for motivated sellers.

Lease Option Case: Steve's First Deal

This study is important because it describes a first deal. I like it because it highlights how each party to the transaction was able to come away as a winner. Here is how Steve described it.

> *Sara had a house in Fowlerville that she kept after her divorce. She couldn't stand to continue living with the memories from the marriage, so she bought another house in Fenton, closer to where she works. She had the house "For Sale by Owner" and "For Rent". She wasn't excited about being a landlord, but she was looking for debt relief in a quick way.*
>
> *I called on her "For Rent" ad and we met to discuss some options. I agreed to start paying her $1,100 per month immediately (because that is what she needed to cover her expenses) and for $1,000 I bought an option to buy at $155,000 sometime within the next three years.*
>
> *I put about $300 into the house to fix a few things, plus a home inspection and title search, so my costs were minimal; around $500.*
>
> *Two days after I signed with the Sara (the owner), a tenant/buyer from my accumulated list paid me an option fee of $5,000 and the first month's rent of $1,195 to move in. The lease term was 18 months and the buy-out was $169,900. There is no lease money being applied to the purchase price. The lease started several months ago and they have been paying every single month early. They have never called me with an issue of any kind, so it is going about as smoothly as I could ever hope.*
>
> *I liked this deal because the owner was very happy that I took the house off of her hands, and she always receives rent from me by the first of the month. The tenant/buyers were very happy because they were able to get themselves and their 3 children from an apartment into a nice house on an acre of land. This is a "win" for me also because I made money on the front end with the option fee of $5,000 plus $95.00 monthly cash flow, and the whole deal will make over $16,000. Not bad for my first deal!*
>
> *S. Giroux - Michigan*

Lease Option Case: The Buyers Provide Cookies

This is a fun story from two of my students who really got off to a great start on their first lease option deal. They did such a great job that their buyer has bought additional properties from them and even sends them Christmas cards and cookies! Here's how they told it.

> *We attended your seminar on Lease Options in Seattle. Within one week of your seminar we located a vacant rental in a nice Seattle neighborhood and were able to negotiate a lease option with the seller. We put the home under contract to purchase it for her full asking price of $175,000. We were willing to pay $190,000 but did not need to go that high. We were to pay $1,000 down, payable in 90 days or when we found a tenant. We pay no interest with 100% of our $900 monthly payment going towards principle reduction. We have three years to cash her out.*
>
> *We sold it on a 1-year lease option in about 10 days for $200,000. That was a great deal for our buyer. We're confident we could have sold it for $220,000.*
>
> *We took $10,000 down, leaving us $9,000 after paying the $1,000 to our seller. We are getting $1,295 a month from our tenant with no rent credit and none going toward reducing their principle. We got a $395 per month positive cash flow for one year that added up to $4,740 + $25,800 after one year when our tenant exercised their option.*
>
> *After making $30,540 on our first deal using the strategies you taught us at a half-day seminar, we signed up for your next 3-day lease option bootcamp and ended up acquiring 19 more properties the following year, and two of them were clients referred to us by our buyer who has now acquired two more rentals from us. Our buyer still sends Christmas cards and cookies and continues to thank us for helping them buy a home when no one would loan them money because of a previous bankruptcy.*
>
> *Thank you for sharing your lease option strategy and inspiring us to jump out of our comfort zones.*
>
> *The Barclay Brothers, Washington*

Lease Option Case: An Investor Reaps What He Sows

This is an interesting case that shows the value of establishing relationships with Realtors®. You may recognize Shaun's name—yes, he is a master of Short Sales himself, but he started out just like you and me (it's good to know different real estate methods so you can turn anything into a deal!).

Shaun got a call from a Realtor® that he had spoken to over a year earlier. She had kept his card. This particular house had been listed for six months without luck. The seller had moved out of state, leaving the home empty for the last four months. Shaun was able to lock in very flexible terms to create a terrific deal for him while relieving the seller of his burden and allowing a new buyer a fresh start.

This deal came as a referral from one of the realtors that I talked to OVER A YEAR AGO!!! She called me out of the blue from my card she had kept. Here are the numbers:

$700.00 per month - Lease option price from seller

$850.00 per month – Lease option price to buyer

$150.00 per month – profit

$132,000.00 Purchase price from seller (for as long as I want… I can buy this house for this price in a month or in ten years; he didn't care either way)

$159,000.00 Sales Price to buyer within 24 months

I also got a $7000.00 option fee from the lady up front.

Not a bad deal, huh? This is almost a $30,000 deal. The great thing about it is that the buyer has pretty decent credit. She could qualify for a loan on this property right now if she wanted to, but is going to wait about a year to get her score up from a previous divorce (her husband had a few late pays). Not only that, but if she doesn't pay me, it's no big deal. I'll just do this whole thing all over again. I also negotiated with the seller that if for any reason I have a tenant that stops paying me that I don't have to make payments until I get another tenant in the property.

This property was listed on the MLS for 6 months at $155K with no luck. The fact that I offered it on a lease option and had a pretty good marketing plan allowed me to get MORE than a realtor could get. (The house was in great overall condition, it was just a little bit outdated compared to the rest of the neighborhood.) The seller had moved to Texas and it was sitting empty for 4 of those six months, so he was obviously motivated.

Thanks for showing me the ropes on this one Wendy! I love it!

Shaun McCloskey, Missouri

Lease Purchase Case: Cleberto Has Multiple Exits

This situation shows that even though Cleberto had an exit in mind when he bought the property, market conditions in combination with the nature of buying on a lease opened up additional opportunities. Cleberto found a property listed with a realtor. It was in a nice area of Orlando where he holds most of his properties. He has a good understanding of the market and home prices there. Recognizing the below market price per square foot, he followed up on the property.

It was a 7-year old home in a nice gated community in Orlando. It had been listed for 2 months at $339,000. The following drew our attention:

The price per square foot was below the subdivision average.

MLS remarks: Motivated seller, $2000 bonus.

Driving by the property we noticed a recent "FOR RENT" sign. Now it was becoming really attractive. We figured the owners must need some cash flow soon, and we wrote our offer accordingly.

After some negotiation, the following was accepted:

1. *A lease purchase at the $339,000 FULL price (to get their attention) for a 2 year term.*
2. *We would advance 3 months' rent.*
3. *Advance $2000 of listing agent's commission (towards purchase price)*

Items a & b payable to owner on or before 60 days

4. *$500 in escrow (towards 1st month rent)*
5. *Rent of $1895*
6. *We also requested that the $2000 bonus offered by owner be paid to listing agent (that way the agent would have $4000 of his commission paid soon)*

We had previously experienced problems taking too long to rent or rent-to-own a property, and had decided for this one to have a fallback plan, in case it was taking too long to market.

Our Lease Option plan to find a buyer was as follows:

1. Rent $1,995 (to move it fast)

2. Option fee of $10,000

3. Price : $379,000 for a 12 month term or $389,000 for an 18 month term

This should give us a profit of more than $35,000 and $45,000 for the 12 and 18 month periods, respectively.

To our surprise, along came someone offering us $2,295 for a straight 12 month lease. We accepted it because it increased our monthly cash flow to $400/month, and there was an up trend in our real estate market. We believed that trend would continue over the next couple of years.

As the end of the current 12 month lease with tenant approaches, the market has experienced the tremendous appreciation as we expected. At this point, these are some of the alternatives we are considering:

> *Sell this property for at least $390,000 and realize more than $40,000 in profit. Comparables are already there to support the price.*
>
> *Put it back on the market as a Lease Option with a price increase of some $40,000, providing a future $70,000 or more in profit.*
>
> *Buy it early from the owner and hold it longer. Since we would be closing earlier, we may request some breaks from them.*

Cleberto, Florida

CHAPTER 3

Finding Motivated Sellers for Lease Options

Motivated sellers are out there in every city, every town, every state. Finding them isn't as difficult as it might seem – if you know which techniques work for attracting the attention of a seller who wants to work with you on a lease option.

I recommend looking for motivated sellers who have nicer homes that require little or no work. This way you spend less time working on the house and less time working to find a good buyer. Also, I like to focus around the median price range and above. In my area, in Michigan, the median price range is currently $120,000 to $170,000 – therefore I have focused on the $100,000 to $200,000 range (so a little below and a little above on each side). These nicer homes are much easier to resell on lease with options, and generally much more profitable than less expensive homes. It's also a lot more fun working on nicer homes for more profit than dumpy homes in rough areas for less profit -- especially when you can buy the nice ones for little or no money down. So how do you find these?

What Makes a Motivated Seller?

There are, of course, different circumstances and situations in the lives of people that motivate them to need to sell their home. This can include job transfer, bankruptcy, foreclosure, upgrading to a bigger home -- any number of reasons. However, the circumstances of the sellers may also be affected by the state of the two vying markets – buyers and sellers – which also affect their motivations. For real estate investors it is crucial to buy homes from truly motivated sellers -- sellers who have an extra urgency, usually financial. You can't get a good deal from a seller that is not motivated, because if they're not motivated, they have no reason to negotiate or give on any part of a transaction.

There are different degrees of motivation and different reasons sellers need to sell their homes, but overall there are two basic categories of motivated sellers:

1. **Desperate and Distressed (bad debt)** – someone in trouble financially, behind on payments, going in a bad direction, short sale, lost their job, divorced, foreclosure, etc or

2. **Stressed but not Distressed (good debt)** – someone not in trouble financially, not behind on payments, but motivated for other reasons: possibility have two house payments, inherited a home, burned out landlord, job transfers, etc.

Most real estate investors only go after #1 above, but there is also huge profit potential with sellers that fall in #2. All of the lease option sellers should usually fall into #2, though that rule isn't set in concrete. In this chapter we will discuss how to find motivated sellers of either type. The final factor likely to affect a seller's level of motivation is the state of the economy itself.

What You Need to Know About Buyer and Seller Markets

The economy plays a big role in finding motivated sellers in different pockets of the country. The economy will be discussed in much more detail later in the book when we cover negotiations, but it is important to understand how it affects motivated sellers. Important definitions are as follows:

Buyer's Market (weak market): when the real estate market is not moving very quickly. There tends to be little or no appreciation, or even depreciation. Sellers tend to be more open-minded to creative ways to sell their homes. There also tends to be higher unemployment in the surrounding area, and overall not a very good economy. **NOTE:** most markets are a buyers market right now in the U.S.

Seller's Market (strong market): a real estate market that is moving very quickly. There tends to be high appreciation. Sellers may be getting multiple offers in one day on their homes, and bidding wars are common. There tends to be a high employment rate in the surrounding area, great retirement/vacation facilities, and an overall good economy.

When the market is very strong, sellers are able to sell their homes more easily, even if they are very distressed. If the market is a buyer's market, it can be very difficult for a seller to sell their home. The odd part about motivation and finding motivated sellers is that no matter what the economy is, a buyer's or seller's market, motivated sellers are always available! You will just need to look harder or you might find fewer in a really strong seller's market, and vise versa in a really strong buyer's market.

Techniques for Finding Motivated Sellers

The kind of motivation you are looking for is not someone just wanting to sell their house but someone who needs to get rid of either their good debt or their bad debt. These sellers won't come knocking on my door, however, nor are they ever obvious. You must try several different approaches and determine what works best in your area. It's a bit like fishing. Try a spot and a lure and see if they work. If they don't work, move to a different spot and try on new lure. Here are some ways that have worked for my students and me over the years:

1. **Bandit signs** – Bandit signs are the small signs you see on the street corners or on telephone poles around your city. They are called bandit signs because in many cities they are illegal to post and you can be fined, but investors still put them out and take the risk of the fine over the potential profit of a deal they may bring. They might say "Cash for Your Home" or "Stop Foreclosure," etc. One of the advantages of buying a house on a busy street is to be able to advertise with a bandit sign in your own yard. Then it *may* not be illegal. Check with your city to see what its ordinance states. An investor I know owns 30 houses in a subdivision. She purposefully bought the one on the busy entrance corner so that she could advertise on the lawn and pull people back into the subdivision to look at the other houses. There are many companies that make these signs and they are not expensive. This way, if you lose them, someone removes them or they blow away, it does not cost you much.

2. **Advertisements in the newspaper** – Generally I find my sellers through ads either they have placed in the paper or ads I have placed in the paper to fish them out. There are several ads that you can run that will attract sellers to call you. Several of my favorite ads are:

Ad #1

```
Company looking for 3-4 homes in
this area for long term lease.
Call 123-456-7890.
```

This ad will draw in the seller that is considering something long term and those that want to rent their home out. In other words, when a person responds to this ad they are ready to do the most important part of an option – lease and do it for a long period of time. This type of person does not need any cash out or they would not respond to this ad. The types of people we really want are the ones that have not been able to sell their home so they are considering *the four letter word*: **RENT**. There is a script that I use later in this chapter for calling the *For Rent* ads in the paper. Use the same script, but only after they call you.

Ad #2

```
Executive looking in this area
for a lease to own - nice home.
Call 123-456-7890.
```

The above ad will draw in the nicer homeowners to call. We are executives in this business, right? I am, and hopefully you are too, so there is nothing disingenuous in this ad. However, the seller will naturally assume you are looking to live in the property. Later, you will need to break the full facts to them slowly. This will be covered when we handle this and other seller's objections.

Ad #3

```
Home not selling? We can help!
We buy and lease homes call
(123)456-7890.
```

Ad #3 will bring in those sellers looking to sell and they are starting to get very motivated. This ad can bring in sellers that are behind on payments or just getting motivated.

Ad #4

```
Tired of Monthly Payments?  We
can help.  Call today – (123)456-
7890.
```

> Ad #4 brings in sellers that are behind on payments – foreclosures, but also those that have two house payments. It brings in sellers with good debt and bad debt. This is a great ad to bring in lease option sellers.

There are many types of ads you can run. Experiment with them in your area. Also use different types of papers. You can try your little local papers or your larger metropolitan area papers depending on your budget and your target market. Also, I have tried some in the *For Rent* section and some in the *For Sale* section depending on the ad.

3. **Tear-off Flyers** in local drug stores, convenience stores, party stores – wherever you can get them posted. These tear off flyers can say the same things as the signs and ads. The tear off parts should have your phone number, website if you have one, and a short statement like "*We Buy Houses*."

4. **Realtors® -** to let them know what type of homes you buy and how you can help them sell their listings. This will be discussed in much more detail when we talk about working with Realtors® in later chapters. This is one of my favorite ways of finding deals. I currently find 90-95% of my sandwich lease options from Realtors.

5. **Long-term M.L.S. Listings** – If you are not a Realtor®, then you can hire a Realtor® to do a search for you of listings on the market of over 90 days or 120 days. These are sellers that are getting motivated because their homes have not sold. Also, you can have them run all the expired listings.

6. **Out-of-State Owners** – There are services in many cities that allow you to find all out-of-state owners, or owners where tax bills are sent to addresses not at the property (non-owner-occupied). Out of state owners are far away from their property and many times want to get rid of the far away headache and move on with their life. Also, they may not really know what the current market is anymore.

7. **Vacant Homes** are an indication that someone is making a payment on a home that is not being used. Find the owner and write them a letter. You can write a letter right to the home and hope it gets answered, or find the owner through the post office, township tax records or hire a skip trace service (you know, a "private eye"). Skip trace services are great ways to find not only sellers that you want to find, but later missing tenants you want to find. They can be fairly inexpensive per search. Check around for a good company that gives good prices and reliable service. Also ask for a recommendation for a skip trace service from a Realtor® or a place that does background checks. You'll start to hear a few names again and again, and you'll be able to make an informed choice.

8. **Real Estate Investor Clubs** (also known as REIAs) always have other investors with homes that they haven't sold or want to sell. Network and let others know what you do. I have bought several very good deals from other investors, either because they had their hands full at the time with their own deals, or they were out of their area. You should be a member of a local real estate investor club and be regularly attending meetings. It is one of the best places to network.

9. **Corporate Relocation Departments** have inventory of homes that have not sold. If the company does not do a *corporate buyout*, then the owners would be great candidates for a lease option. They have relocated and need to have someone in that home and making payments.

10. **Your Local Chamber of Commerce** can tell you what businesses are leaving, who is coming in, etc. If you have many properties, they might also list you as a rental company and refer incoming people in the area to call you.

11. **Word of Mouth**. After you have been in this business and networked over a few years, you will start to get deals brought to you by word of mouth. Someone knows someone that knows that you buy homes. I have bought some of my most profitable homes from word of mouth.

There are many ways to find sellers and get lease option deals, but my favorite ways are:

1) Calling Sellers right from Craigslist or the newspaper
2) Working with Real Estate Agents

Motivated Landlords

Landlords can be great motivated sellers, especially if they are burned out. If the economy is slow, they might have higher vacancies than in a fast or hot market. In my experience, I have found there are two basic types of burned out landlords:

1. The one that has watched a lot of late night TV and decided to make their millions in real estate.

Unfortunately, there are many people that buy real estate with no knowledge or experience. They think they know it all after a high-powered, adrenaline-rushed sales pitch. There are, however, many state and federal laws that regulate this business. This type of landlord will fall for the professional tenants and their stories and experience, and often end up getting burned.

Understanding how to screen tenants and select them is key not only to being a good landlord, but also the business of selling using lease options. By being a member of a local real estate group, investors will get the education and assistance they need to be successful as an investor. If you want to find a group in your area you can check the National Real Estate Investors Association website – in the back of the book for a group in your area.

2. The second type of landlord is not really "burned" like the first type of landlord, but they are retiring and moving on with their life. They don't need the money from the sale of a home, and in many cases they don't want it yet. They usually have huge capital gains to

contend with, and may not want to pay those gains yet, or they may want to plan for a 1031 exchange.* [A 1031 exchange is an IRS section that allows a person to *exchange* their kind of property to another like kind of property, of equal or greater value, and therefore defer (not avoid) the capital gains on the first property. For instance if a seller has a home that they bought 10 years ago for $80,000 and it is now worth $140,000 and they have depreciated the property from $80,000 down to $40,000 then there is a $100,000 gain they need to realize ($140,000 value less the depreciated value of $40,000 = $100,000 of gain). This would be a long-term capital gain, but many sellers still don't want to pay on this amount. By optioning their home to you, they might be able to better plan for a 1031 tax deferred exchange. There are sellers that will sell to you on an option to avoid the taxes now but like the benefits of renting their homes. They like the cash flow and with this solution they can still benefit from cash flow and avoid the other issues of being a landlord that they don't like or won't have time for now.

When I purchase a home from a landlord, one of the benefits to him or her is that I will usually assume the maintenance completely on the home, or ask them to assume only the first $500. I also will take on the advertising, vacancies, and showings, etc. You can be very creative when structuring a deal with an owner of a home. The benefits for a landlord include but don't have to be limited to:

A. *Maintenance* - sellers don't have to deal with issues and calls. Even if they pay a portion of the costs, I will handle the work.

B. *Showings* - sellers never have to show the home again. I will do the showings, take the calls and discuss the home with all tenant prospects.

C. *On Time Rent* – they don't have to worry about the tenant paying each month. Their rent check comes from me *regardless of whether or not the tenant has paid me on time*. My check is good and on time each month.

D. *Advertising* – they don't have to advertise the home anymore. I will pay for all the adverting and handle all of the calls.

E. *Vacancies* – they don't have to worry about vacancies anymore. I will pay whether the home is vacant or not. [You can negotiate this also if the seller is willing – e.g. you have one month free rent in each X (any number you choose) months of the lease if you don't have it occupied (all contracts with landlords are negotiable, but you should only negotiate with them to pay rent in a slower market, a buyer's market)].

F. *Insurance* – they have extra liability protection when they lease option to me. I carry a $1,000,000 liability policy on properties that I don't own and am only optioning. This liability policy is really to protect me, however, if something really bad were to happen on this property, this insurance would be utilized in a defense, which would also protect the owner of the home.

These benefits alone will allow a landlord to feel comfortable with selling, but also allow them to take less in rent then they usually receive. Talk about these benefits to help them see the advantage in leasing the home to you with an option. They now have less headaches, overhead, fees and expenses, so they can lease it for less. With a lower payment to the seller, you can also rent it to someone and increase your cash flow. It is hard to determine the exact amount to reduce their normal rent because there are many factors, but normally several hundred per month or more is reasonable.

How to Evaluate Seller Ads in the Newspaper

Besides placing your own ads in the newspaper to attract sellers, you can also answer their ads. In lease options I find that most sellers need or want their cash out. The best way to find a seller for a lease option is not the FSBO section of the newspaper, but the *For Rent* section of the newspaper. What you will want to do is to turn the landlord into a seller.

Your first step is to build rapport.

Call the ads in the paper that are in the *For Rent* section, not the *For Sale* section. The reason I don't call the "For Sale" section is that 90% or more of those sellers must get their cash out and a large portion of the other 10% won't consider something creative. It is not because they don't want to consider something creative, it is just that they would prefer to cash out and be done with the property. Also, trying something unique will scare most sellers. Call the ads that are for rent, because the #1 and #2 objections for selling on an option have been resolved: 1) they are renting, and 2) these owners do not need to sell or to cash out of the home and they are willing to lease the home.

Wendy's Tip

One trick to finding motivated sellers is to take the current real estate section of your newspaper and file it in your cabinet for a month. After a month, start calling those sellers. If their home is still available, then they are getting more motivated. The longer their home sits on the market, the more motivated they become.

How to Navigate Successful First Contact with Sellers

The most effective way to contact sellers is by calling them. Immediately tell them your name to start building rapport, and try to keep your voice sincere or soft. Be sure to ask questions appropriate to the area you are calling. What is important to that part of the country? Basement? Pool? Fenced yard? A certain type of landscaping? Updated kitchen or bathroom?

When you begin to regularly respond to seller ads, consider setting up another phone line, perhaps toll free or even a voicemail box just for that particular house or ad. Personally, I prefer for callers to reach a live person, so if they call my office they get someone live. You can always use your cell phone. Even if after hours, they will get a referral to another number where they can get a live person. However, if this is not feasible for you, be sure to check messages frequently and return calls promptly.

The following is a script you can use to call an owner of a rental home. The words in bold are what is said to the owner. Don't waste the seller's time asking questions that are answered in the ad or from their description above but do ask questions applicable to your area of the country (e.g. Is it in a flood area? Does it have central air? Has it ever had termites? Has it ever been in a fire? How old is the roof?). Ask whatever might be of interest to you and to find out more about the home.

Script for Calling the For Rent Ads

Hi, my name is ________. I was calling about your home for rent.

Giving your name sounds warmer and will help put the owner at ease with you. It is a great way to build rapport.

Can you tell me if it is still available?

If yes, continue.

When is it available?

Can you tell me a little about the home?

Let them answer some information about the home…or expand some questions off the ad. You are building rapport with the owner. Talk and *let them talk*. People warm up when they are the ones talking. Listen and sound interested.

When was the home built?

This question gives you insight to any decorating or maintenance problems you might be running into. It will tell you if it might need to be updated. If the house is older, ask the next question; if not, skip it.

Have the kitchen and bath(s) been updated since it was built?

If it was built in the 70s, I might ask if the baths or kitchens are yellow/green/brown or if they have been updated since it was built.

Does it have a garage or basement?

Is the yard fenced?

This may prompt them to ask the question on whether or not you have pets. At this point they still think you are the one that will be living there. I don't change that direction of thought until enough rapport and trust have been developed. They may ask questions as to how many will be living in the home. These are questions I don't want to lie about, but don't want to be totally direct on either. If you say, "I don't know, I am going to rent it to someone else," you can be sure they will not show you the home. That would kill the trust and rapport immediately. It is hard to say how to handle those questions exactly. Each time these questions come up, you will be answering them differently based on the owner. Here are some ways you could consider handling their questions to you:

1. Answer them as if you really were going to live there. The answers would be of you and your family (if any).
2. Try to change the subject or slightly avoid the question.
3. Try to answer to your best guess of who might be renting from you later.
4. Just come out with it: “Actually, I am working with a few local families to help them find a nice home in a nice neighborhood, is your home a nice home in a nice neighborhood?” - this works very well and now you have disclosed you are an investor without saying “I am a real estate investor”.

I am not recommending deliberate deception although it may sound like that. I am very honest and straightforward with my sellers but I need to build rapport—not scare them off. I later reveal how this will work after they meet me or when I feel that they are open to discussion about the entire situation. Because everything will eventually be in writing, they will know that you are not occupying the residence before they sign the documents.

If the home sounds like something you would like to own then pop the question. If it doesn’t just be polite and say you will call back later if you are interested. ***Thank you very much.***

Wow, this home sounds really nice, would you considering selling it?

If they say no, then say, “Thanks, but I am really looking for something I can buy.” Leave them your name and number to contact you later if they change their mind about selling.

Do you know how much you would want for the home?

Start to feel out the owner for the type of terms they would consider but be careful not to make any verbal offers. This isn’t the time for negotiation. This is still just the time for gathering information. You need to construct your offer when you are not on the spot.

When could I come and look at the home to see if I would be interested in it?

If the home is available for viewing, make arrangements to go as soon as possible. This shows the seller that you have more than casual interest in the property. Set a time with the seller and keep it. If you must change your schedule, be sure to let the seller know and make alternate arrangements for as close to the original date as possible. This will also show the seller that you are interested enough to be courteous.

I will challenge you to call 10 for rent ads today and follow this script. If you get some leads and need help, consider my coaching and courses. You can email me at info@wendypatton.com. You have now called sellers, had sellers call you, and perhaps you’ve accumulated some leads to pursue. Now it’s time to go look at the homes, continue to build rapport with the sellers, and gather more details on the homes. In the next chapter, you will learn more about which tool/technique to use for each motivated seller you have found.

CHAPTER 4

Evaluating the Profitability of the Deal

Winner: Stupidest Moves Award

One of the investor groups I used to be involved with used to give away awards called the "Stupidest Moves Award" for the person who makes the most ridiculous, stupid real estate move during the year. Actually, they give away lots of different awards for silly things investors do during the year. I didn't even know this award existed until I got it, and the only reason I got it was because I was chatting away about my deals to other investors. I received a mechanical shark, mounted on a plaque, that was devouring a large monopoly denomination, to depict the eating away of huge profits.

It was the early 90's, and one of my earliest deals with a Realtor®. I was presented with a great deal for a $300,000 lakefront home. I felt I could rent it easily because of its price range and because it was lakefront property. Therefore, I quickly committed to start my option on October 1st, whether or not I had secured a tenant/buyer. My rent commitment was $1,400 per month, and of course I planned to charge more in order to make cash flow. October turned into November, November into December, December into January, and January into February.

Unfortunately in Michigan lakefront properties are not very desirable in the middle of winter. I finally rented it in March. In total I lost more than $7,000 plus utilities for the winter. I was paying more for a house I wasn't living in than for my own mortgage.

I could have avoided winning this award by either:

1) making my contract contingent on securing a tenant, or

2) waiting until spring to start the lease option.

Lakefronts rent the best in the spring and summer in my area. People aren't crazy about moving into a property with a frozen piece of water in their backyard; water which may not thaw for months. I was too eager and didn't think it all the way through. Not only did I lose over $7,000 in profit - it was $7,000 worth of cash out of my pocket. Although I made well over $25,000, it could have been $32,000 with much less stress. That's how I earned the "Stupidest Moves Award" in my investment group. That's really not the kind of award you want to repeat, but everyone has a story like that in their investment portfolio. It's just part of the learning process.

Eagerness to start a deal should never outweigh the time needed for thoughtful preparation in evaluation and construction of an offer. There are many sellers willing to sell using a lease option, but they must be profitable for you!

Wendy's Tip

Know your climate. People don't like to move in the winter in a colder climate, so if you live in a place with bone-chilling winters, structure your deals, if possible, to start and end in the spring or summer. Also, try to work around holiday months, especially mid-November and December everywhere in the country. All of my contracts to buy don't start until I find someone to rent from me. I learned this one the hard way.

Creating the Offer

Now that you've considered using the lease option technique, you need to step back and take the time to work out the profitability of the deal. Normally you should not throw out numbers to the seller in the excitement of the moment. Even if they are pressuring you, inform them that you'll need to go back to your office and crunch the numbers. In the excitement of the moment you may voice a dollar figure that doesn't include all the things you need to consider. In the quiet of your office you will have the time to go through your own **profitability worksheet** discussed in this chapter and make sure the numbers work for you. Negotiations and offers are an art form.

Lease option offers, by their nature, rarely require an on-the-spot response. Therefore, you can respond according to the dictates of each specific situation. There may, however, be situations where you'll need to respond immediately. This need may arise most commonly in the case of a subject-to offer on a pre-foreclosure or other competitive bidding situation.

Calculating Your Profit Requirement: Sandwich vs. Cooperative Lease Options

As an investor you must determine your profit requirement for any given deal. It may vary depending on the type of investment. For instance, I will accept less for a cooperative lease option than a sandwich lease option because I can be in and out of a cooperative very fast; sandwich lease option transactions typically require 18-24 months or more. Is your profit requirement for a deal $10,000, $50,000 or what? Once you determine your profit requirement, that becomes the bottom line number that must be reached in order to take on a transaction.

For example, if your required profit is $20,000, and an opportunity comes along that will only provide you with $18,000, then you'll either need to negotiate the terms of the deal with the seller to meet the $20,000 requirement, or pass up the deal. It will not be a win/win situation for the seller and yourself. This is when a **Cooperative Lease Option** may work. See my website for an article on this technique.

There are times when a seller will do only X, Y, and Z. (X, Y, & Z, being price, payment and length of time). You can input those numbers into your spreadsheet below to determine if it meets your profit requirement. If it does, you can do the deal. Sometimes, if it doesn't you can still negotiate a little further as discussed in the next chapter. Also, many times the seller is not always set on X, Y AND Z, just X and Y, therefore you can negotiate the Z. The next chapter will help you think of some creative ways to help bring deals together. However, there are some deals where you will need to just walk away. Some sellers are just not willing to do what you will need to make it a win/win, and some sellers are not motivated enough or can't go down on price enough because they owe too much. Learn to move on quickly and look for another motivated seller. Wasted time is money to you, and you must move on to another motivated seller if the deal doesn't work for you.

Profitability for Sandwich Lease Options

The first thing you will need to do is to create a worksheet for profitability for a Sandwich Lease Option.

Appreciation or depreciation is not something you can be exactly sure of, and therefore, will need to be predicted or somewhat guessed. The newspapers will be a great source for the appreciation rates in your area. Base your estimates on the predictions of your local writers or Realtor® boards. When calculating the option premium I use 5% because the appraisal market is so tight right now. When appraisals are loose, or the comparables are wide in their price range, I might use 10%. This is not appreciation, but an additional bonus we get because we are selling to our buyers on terms.

Cash Flow or Rental Value is something you will also need to evaluate and determine. You will need to do rental comparables just like you do sales comparables. Here are ways to find the rental comparables:

1. Read the local paper. Check the all the local rentals. Those are your *comps* = comparables.
2. Check with people in your local landlord group – many rentals are not on the MLS.
3. Not enough data in #1 and #2? Run a test ad in the newspaper or on Craigslist. Too many calls? Your price might be too low. Not enough? Your price might be too high. It's a little like fishing.

Worksheet for Profitability for a Sandwich Lease Option	
Purchase Price	$
Expected Sale Price	$
Current Value: _____________	$
5-10% value of lease option (premium) Current appreciation:________	$
Cash flow per month ________ x____ mo.	$
Your Rent vs. Market Rent	$
Other Benefits:	$
Total profit of the deal:	$

Example #1: Sandwich Lease Option

Let's look at the facts:

- Seller will sell you their home for $185,000. It is currently worth $190,000.
- The appreciation rate is 5 percent per year.

- It will be an 18-month option, which will result in 7.5 percent appreciation (5 percent x 1.5 = 7.5 percent). That gives us $14,250 ($190,000 x 7.5 percent) of appreciation value during the 18 months.
- You'll pay the owner $1,300 in rent. You can rent it out for $1,600, for a cash flow of $300 per month.
- Note: I usually rent a home for $1,595 vs. $1,600 because $1,595 sounds less than $1,600, but it is easier to show even numbers for the examples.
- All of the homes in this neighborhood are diverse and unique. Prices range from $170,000 - $285,000. This allows us to build in a higher option premium at 10 percent or $19,000.
- The $19,000 option premium and the $14,250 appreciation adds an additional $33,250 to the retail value of the home.

What is your estimated profit in 18 months? Let's view how I would figure out the profit of this deal:

Profitability Worksheet Sandwich Lease Option	**Example 1**	
Purchase Costs		Totals
Purchase Price	$ (185,000)	
Total Purchase Costs	$ (185,000)	$ (185,000)
Income Sources		
Current value ($5,000 above purchase price)	$ 190,000	
Value of Lease Option (10%)	$ 19,000	
Expected Appreciation (5% annually, 7.5% over 18 months)	$ 14,250	
Expected Sale Price	$ 223,250	$ 223,250
Expected Monthly Cash Flow ($300 per month for 18 months)	$ 5,400	
Total Other Income	$ 5,400	$ 5,400
Expected Profit		$ 43,650

The resulting profit from this deal if all payments were made during this option period and it went the full 18 months would be approximately $43,650, less transfer fees, title, insurance and possible option credits from the investor to the tenant buyer. Does this meet your required profit? If so, then move forward with these terms. If not, you continue negotiations on the deal or pass it up.

Example #2 – Sandwich Lease Option

Let's look at the facts:

- Seller will sell you their home for $145,000 on a 12-month option. It is worth $145,000.
- The appreciation rate is 3 percent per year which will result in an additional $4,350 ($145,000 X 3 percent) after one year.
- This home is in an area where all the homes are very similar and range in price from $140,000 – 152,000. This will result in a more modest option premium of only 5 percent compared to the 10% premium in the prior example, or $7,250 ($145,000 X 5 percent).
- The appreciation and the option premium are $11,600 ($4,350 + 7,250).
- You'll pay the owner $1,000 in rent and will in turn rent it out for $1,200.
- The seller is willing to give you $200 a month credit towards buying this home.
- NOTE: if you have depreciation then you subtract that number (very possible it can go either way, but this example shows appreciation)

What's your estimated 12-month profit:

Profitability Worksheet Sandwich Lease Option	**Example 2**	
Purchase Costs		Totals
Purchase Price	$ (145,000)	
Total Purchase Costs	$ (145,000)	$ (145,000)
Income Sources		
Current value (same as purchase price)	$ 145,000	
Value of Lease Option (5%)	$ 7,250	
Expected Appreciation (3% annually)	$ 4,350	
Expected Sale Price	$ 156,600	$ 156,600
Expected Monthly Cash Flow ($200 per month for 12 months)	$ 2,400	
Option Credit from Seller ($200 per month for 12 months)	$ 2,400	
Total Other Income	$ 4,800	$ 4,800
Expected Profit		$16,400

This deal would not be nearly as profitable for an investor. It would only generate $16,400 before closing costs, not leaving much room for potential problems. This opportunity does not meet my minimum profit requirement for a sandwich lease option. However, there are ways to renegotiate the deal with the seller. With the appreciation this low it must be more of a buyer's market. You should be able to:

- **Negotiate price and terms**: Ask for a better price and for additional monthly credit towards the purchase.
- **Ask for the equity buy down** of the mortgage during the option period. For example, if the seller owes $100,000 on their home at the start of this option and at the end they only owe $90,000, then you would receive the $10,000 of credit that was paid on the mortgage balance during the option period, because in effect you had been paying that mortgage payment during the option period.

If the seller would not agree to the additional terms, I would gladly let it sit until it makes sense for them to agree to terms that would make this transaction meet your profit requirement or consider a cooperative lease option. In any case it must meet your bottom line number and result in a win for you and the seller. Let it sit until their motivation increases. It can take months, but patience pays off.

Example #3 - Sandwich Lease Option

Let's look at the facts:

- Seller has a home worth $235,000 and will sell it to you for $225,000 on an 18-month option.
- The appreciation rate is 5 percent per year (or 7.5 percent over 18 months) which would generate an additional $17,625. This home is in a very diverse area out in the country.
- The homes range in square footage and acreage.
- Prices range from $150,000 - $450,000.
- These factors let us establish the option premium at 10 percent or $23,500.
- The rent you pay the owner is $1,200, and the market rent you expect to receive is $1,450.
- The seller owes $150,000 on their mortgage and agrees to take $75,000, less closing costs, at the time of closing ($225,000 sales price less $150,000 current mortgage balance). This allows you get the mortgage equity during the option period. The equity from the principal pay down during this option period is estimated at about $200 per month or $3,600.

What is your estimated profit in 18 months?

Profitability Worksheet Lease Option	**Example 3**	
Purchase Costs		Totals
Purchase Price	$(225,000)	
Total Purchase Costs	$(225,000)	$(225,000)
Income Sources		
Current value ($10,000 above purchase price)	$ 235,000	
Value of Lease Option (10%)	$ 23,500	
Expected Appreciation (5% annually, 7.5% over 18 months)	$ 17,625	
Expected Sale Price	$ 276,125	$ 276,125
Expected Monthly Cash Flow ($250 per month for 18 months)	$ 4,500	
Expected Monthly Equity ($200 per month for 18 months)	$ 3,600	
Total Other Income	$ 8,100	$ 8,100
Expected Profit		$ 59,225

Note there are no commissions being paid to Realtors in these examples. Discussions of working with Realtors will be handled in later chapters, however, *if you are paying any type of Realtor commission or option fee up front to your seller, then you will have some out of pocket costs. This will not affect your bottom line profitability, as option fees are applied to the purchase price at closing, but it will affect your upfront cash out of pocket.*

Which of the three scenarios will get you to financial freedom? The answer is that they all can if you do them correctly. Example # 2 would probably require changes from the seller to make it work for you.

The primary profit source is the back end - the difference between the purchase price and your selling price that is realized at closing at the end of the lease option period. When you're first starting out, you might make deals with smaller backends. That's fine. Those deals help you learn the business. As you become more skilled in working with options, you will find more ways of improving the numbers to get you higher returns that are still a win/win. Obviously the higher the backend, the easier it will be to begin working your way towards your financial goals.

Wendy's Tip

There are always unexpected costs in any deal and, therefore, I like to make sure that I always have extra profit built in to any real estate transaction.

Always plan for something that *could* go wrong. There will always be someone that won't pay rent, a furnace that goes out, a roof that leaks, a septic field that fails, etc. Plan for the worse and you will be safe.

CHAPTER 5

Negotiating the Deal

Steps to Buying on Lease Options

Build Rapport and Make a Deal!

In one house I visited for a potential purchase, the woman had a lot of birdcages in her garage, and all of them had price tags. Either she was about to have a garage sale, or she had already had a fairly unsuccessful one. I didn't know anything about birds, but I had this crazy thought that I could get a parrot and teach it to say, "Hi, welcome to Majestic Realty" when people came through the office doors. The idea fell through rather quickly when she told me that birds pick up almost everything they hear you say. I could just hear the bird saying things they heard from my office staff when they hang up the phone from tenant calls. "Yeah, that tenant is lying." "Liar, Liar!" "Yeah, Grandma died again!" I could write another book on tenant excuses (couldn't we all?).

Nevertheless, I continued to chat with the seller about different types of birds while looking around at the house. It's an example of how to learn and build rapport with a seller. People like to talk about what is important to them. It makes them feel more comfortable with you. One of the cages was marked $20 and I decided to purchase it. I thought perhaps one day I'd get a bird, but I couldn't take the cage with me at that time because it was rather large and wouldn't have fit in my car. I told her that I'd send some of my work crew back that evening to pick it up; they had a truck. At this time, we were in a strong sellers market, and I already had a tenant buyer who wanted to buy the home. I was going to purchase this home outright directly from the market. Our market was VERY hot! So I made an offer through the Realtor®, the very first day, and the Realtor® called me up that evening and said, "Well, we have another offer".

I had figured it was very possible, so I simply responded "Oh..." Homes don't stay on the market long in a hot market, especially in that price range, and that home had just come on the market that morning. But she continued, "Let me tell you the stupidest thing I've ever heard."

I said, "What?"

The Realtor said, somewhat angrily, "Well, she accepted your offer."

I asked, "Well, why is that so stupid?"

"Because the other offer was $5,000 more than yours with the same terms and that's just stupid to me, Wendy. But do you know why she accepted yours? She likes you."

Did the bird cage discussion save me $5,000 or did it get me the house? I think it did both. I didn't buy the cage to get the house, but everything you can do to make a prospective seller feel comfortable with you will ultimately be worth it. I always tell my students that if they are not comfortable building rapport with sellers to send someone else, because it is such a crucial element to succeeding in this business. That seller was not in a position where she could just give away $5,000, yet it was important enough for her to sell her home to someone she liked and felt good about that she took $5,000 off of her price. Make it a point to establish rapport and you will almost always get a better deal.

How to Build Rapport with a Seller

If you were trying to sell your house, who would you give a better price to? The buyer who comes in saying…

> "I don't like your carpet color. Are you going to replace it?"

> "The walls won't match my furniture… this kitchen is just not my style…"

…as opposed to the potential buyer who says, "I like the layout. I see there's a small ding in this wall. You don't mind if I fix that, do you? I just want to make this my home. I love it." The 2nd person, of course, because they are reasonable and appear they are trying to work with you. You would instinctively want to work with them.

> **Wendy's Tip**
>
> When you're in the seller's house, tell them what you like about their house, not what you don't like. For example, perhaps you'll see something unusual, like older woodwork or a nice fireplace. Ask the seller about it. If you see the seller likes golf, talk golf whether you like golf or not.
>
> Always focus on the positives, the interesting things. People like to know you like their house, and that builds immediate rapport.

Building rapport with the seller is key to making a deal. If the seller (or Realtor®) doesn't like you, the deal will probably never happen. Therefore, if meeting people and being reasonably conversational and interested in the seller's home isn't your strength, take someone with you who is warm and friendly and can bridge that gap for you. The reason this is so important is because for a lease option transaction you're asking someone to give you control of their house with little or no money down. They must feel comfortable with you.

While it's still important to establish rapport in a rehab situation, it's also appropriate to point out problems in the property. You will need the seller to be prepared for your lower offer when it comes. You have to offer lower prices when using other techniques and not buying with terms like a lease option. Buying at a low price is more critical to your profitability when doing a rehab and sale than when taking control of a property and holding via a lease option approach. In a lease option, emphasize the positive, you will want the seller on your side.

The Basics

I start out with rapport-building questions. I quickly look around the house as I enter and look for items from children or pets, something of significance, maybe a hobby or a collection. Anything that I can use to talk about something of interest other than just the house itself.

Once I spot something I ask about the particular items. Maybe it's a spoon collection or a rack of golf balls from different courses—whatever! What I'm looking to do is to get everyone to lighten up and talking about something significant in their life.

It's not until after that do I guise the conversation around and I ask the following question, "What is it that you're trying to accomplish with the house as a result of my help?"

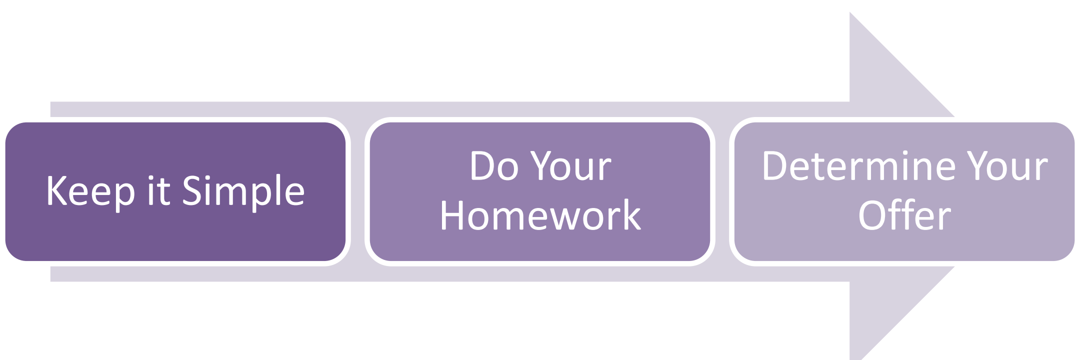
[Note: Use the word *house*, not *home*. You want to separate out the touchy, feely, warm and fuzzy of their home.]

And then *shut up and listen*, acknowledging that you understand with your facial expressions and body language. I want them to see that I honestly care about them and their situation (and I do - if the deal isn't right for them, I won't do it). This will pay off huge returns when we start talking about the terms of the deal. They don't care that I've been in real estate for over 25 years and they don't care that I've done over a thousand deals. They don't care that I taught the loss mitigation for the third largest diversified lender in America how to work with investors. What they care about is if I can help them with the problem that's in front of them.

An entire book could easily be written on *negotiations* with sellers, but those have already been written. Read those books to get more details on negotiating and the psychology of negotiating. Some of them have really helped me over the years understand people and why negotiating itself is so important to completing a deal. This chapter will give you ideas specifically on building rapport with sellers, presenting informal proposals to sellers, negotiating terms, and handling their questions and objections for lease options.

Putting Together the Proposal/Offer to the Seller

Steps for a Proposal/Offer to the Seller



1: Keep It Simple

Sometimes we get too formal – wanting the proper letterhead and business cards and looking too official up front. This is natural, because we feel it gives us the legitimacy a seller expects. However, counter-intuitively, there are times when too much polish may in fact be detrimental to the seller who finds it impersonal.

Save the formal documents for when the deal is negotiated and needs to be drawn up in detail. For preliminary proposals it's best to outline several scenarios, even hand-written. There are many deals made on bar napkins, and they are legitimate and legal as long as they are signed. It's all about personal relationships, not just professionalism. The seller needs to like YOU, not your business card.

Putting out an offer is a lot like fishing. We're trying to find out what's important to the seller, where they are financially, whether they need their cash out and what terms will work for them. If the seller is not sure, then you can use the proposal format in chapter 11 and give them a few scenarios in writing to help them evaluate different alternatives.

Many times they will know what areas are most important to them. For instance, price might be the most important area to a seller. You then can work around price by negotiating the other areas of terms to make the deal work for you. You will have to tweak the other areas of the lease option in order to get your profit requirements, but at least you know where the seller is starting. You know where they are firm and what is important to them. This is where you will need to go back to chapter 5 and use the profitability worksheets to make sure that the numbers will work for you.

When you agree on the terms with the seller, then you should formalize the contracts. When you think there is going to be a meeting of the minds, or if the Realtor® says they want everything in writing, or if the seller says "I want to see every piece of the contract before I agree," then I put everything together, but initially I just put together a simple proposal or we discuss it verbally. This will all be based on the seller and how they prefer it. Many times they like to just discuss it and sometimes they want it in writing. When a seller says they want to see it in writing, they may be referring to a proposal, unless they have said the entire contact and they are clear and ready to move forward, otherwise I would start with the proposal first. There are also times when timing is critical and negotiations must be done quickly and contracts are also drawn immediately.

2. Do Your Homework

You can't put together a proposal without first doing some research, especially if you are in an area of town that is new to you. You can't base your offer purely on what you think the home is worth; you must incorporate the comparables as well. You will need to find out at what level of similar homes in the area are worth by either checking the newspaper or using the MLS.

The MLS (Multiple Listing Service) is protected by Realtors® in most areas of the country. However, it is available to the public in some parts of the country. You would need to ask investors in your local real estate investor club the status of the MLS in your area. If you have a relationship with a Realtor®, you can ask them what the comparables (comparable market values) are in a certain neighborhood.

Understanding the current economy is essential to making offers on lease options work, and work effectively. For instance, are you in a strong buyers or sellers market? Understanding the differences and how they affect the sellers is key to successful negotiations. These techniques will work in either a buyer's or seller's market; however, it is important to know which market you are in so that you can establish your offer correctly. These markets were discussed in detail in Chapter 3, but it is important to realize that in negotiations they will play a major role.

Offers in a Strong Sellers Market

In a seller's market, you're going to buy for a higher price. When things are appreciating in a seller's market, I would have no problem paying closer to retail for a property. There are times when you could pay higher than retail and still be profitable based on favorable appreciation and other terms. You must work the numbers yourself. Your value in the property is not only going to come from the appreciation but also from the lease option when you sell.

Offers in a Strong Buyers Market

The opposite is true in a buyer's market. The economy is slow, likely with higher unemployment rates. Real estate listings aren't moving, in which case you need to buy low -- meaning below the retail value – because you can't count on appreciation. When the market is slow, the buyers have less money and are less able to take on more debt. The advantage of the buyer's market is that you can cherry-pick your deals.

You must remember this in negotiating with your sellers: if your sellers are unwilling to give, you have to move on. They are not the motivated sellers that we discussed in Chapter 3. The slower the market, the more you can negotiate. As more properties are languishing on the market there is a large pool of motivated sellers for you to choose from. You can be selective in order to find deals that work out for you and the seller.

3. How to Determine Your Offer

Potential Areas to Negotiate for a Lease Option

Options are such beautiful tools with which to buy and sell properties. While there are too many variations to discuss in detail, we will cover the key areas available for negotiation. When structuring your lease option with the seller it is important to understand which of these criteria is most important for them:

- Price
- Length of Contract
- Monthly Payments
- Option Credits
- Mortgage Buy Down – The principal adjustment
- Automatic Renewal Periods

In addition to the criteria discussed above, **I usually include terms that will limit my risk.** One such approach is to include a clause that says my lease option can be terminated within 60 days with written notice to the owner. This provides an agreeable exit to problematic transactions.

Another method that I use even more frequently is to make the start of the lease option contract subject to finding a tenant buyer. This significantly reduces your overall risk and prevents you from having to begin funding monthly payments before you have your own funding source in place (unless you want to run the risk of winning the shark trophy I mentioned earlier!).

Multiple Offers

Sometimes you will need to create multiple offers on the same property. This is not unusual. For example, let's say I make an offer of three years at $225,000 and pay the seller $1,000 per month. The seller then looks at appreciation rates and says they don't want to lose out on all the appreciation in the next three years that I will profit from. So, I then restructure a second offer where I might offer to go five years and give them a little more on the sales price as well as a little more each month, but they have to agree to all five years.

You might also want to do a step approach based on appreciation with a lower percentage than the market appreciation, so that you aren't giving away the entire profit. For example, one time I purchased a home from a seller that wanted part of the appreciation, which at that time was 10 percent per year. I asked him how much he was expecting. He had responded with 2 percent per year. I felt that was fair and therefore, we settled on him receiving part of the appreciation and me receiving most of it. You can still give away part of the profit and make it a win/win.

When objections arise, put yourself in the seller's shoes and reflect on what they say. Always try to come up with creative solutions to keep the discussion going. Find out what their concern is, and if you can fix it, say, "If I could do that for you, would you do the deal this way?"

Find the seller's key issues so that you know what terms are more flexible for them. **Whenever you give up something, negotiate something back in return.** With a seller, usually the first question asked is the most important question to them. If they mention 2-3 different issues, find out which is the most important.

Find the Seller's Sticking Point

Sellers will have something that means more to them than anything else. Find out what this is so that you can structure a deal that makes them happy while simultaneously meeting your requirements for profitability. For instance, the price of the home may be more important to some sellers than when they get the price.

For other sellers, they might want a certain monthly payment but their price is negotiable. Sellers have an area that is the most important to them when selling their home. Work with each seller to understand what "makes them tick," so that you can tailor an offer to suit them best.

Handling Lease Option Sellers’ Objections and Responses

When you provide your proposals, sometimes the sellers will accept, and other times they will shake their head and walk away. It’s best to soft-pedal their rejection with a comment such as, “Well, things might change for you, so please give me a call somewhere down the line if you’re still interested.” Many do come back to me that way. Sometimes people don’t want to act today because it’s not a win/win for them, but a few months down the road they’re feeling much more motivated. Always handle sellers graciously and be accessible. You never know when they will call back and say, “Ok, we now want to accept the proposal that you presented us a while back”.

Wendy’s Tip

Time always increases motivation. Sometimes if it’s not a win/win for the seller now, it may be in a month or two.

Some sellers like to feel like they’re dealing with an individual rather than a company, and yet some like to know it is a company and not just one person. Each seller is different and you will need to know how to read sellers and accommodate them. It’s more personal, and the more personal you can be with a seller, the better they will feel about making the deal. Of course, when the paperwork comes through, it will have my company name, but when I’m talking with the seller it’s just between them and me.

Overcoming Sellers Objections

If you have properly built rapport and trust with the seller first, their objections should be minimal, and can be handled confidently and easily. Too many seller objections usually mean you have a seller that is really not as motivated as you may have thought, however, they may just have questions that need to be answered.

Learn to LOVE objections. Objections are buying signals. What the sellers are saying by coming up with objections is that they need more information before they can make a buying decision. When they have objections, they want more information!

I have gotten to the end of my presentation and the homeowner had no objections, yet still didn’t get the home. I obviously missed either asking the correct question or didn’t pick up on the homeowner’s hot button. There are only so many objections sellers can have and once you have overcome any particular objection that is now in your repertoire. Once I’ve addressed an objection, I can’t wait for that question to come up again.

One technique in dealing with seller objections is to feedback their question. Many times we think we understand the question and the intent was something else entirely. Example:

They say, "Your offer isn't enough!"

I reply, "My offer isn't enough?" Then look at them and **don't say another word.**

What I'm trying to do is see if the question is a smoke screen or if there is another objection. It could be that my offer isn't enough money up front; it could be that my offer is for too many years. By feeding it back I put the ball in their court and can get more information so that I can give them a correct answer and not bring up another objection they hadn't thought of.

Wendy's Tidbit

Learn to LOVE objections – They are buying signals!

There are, however, a few objections and questions that you need to be prepared to handle. Here are my recommendations on how to handle each of these objections and questions.

Objection #1: I don't want tenants in my home

Possible Solution: The #1 objection for sellers who are doing FSBOs is that they don't want tenants in their home. They need to understand that future home buyers are people who want a home to take care of. Let the seller know that you understand they might be concerned about tenants in their home. *"I want you to know that I really screen my tenants and they are hand selected by me. I also am not going to put just any 'tenant' into your home. I am putting a **future home buyer** in your home. This type of tenant takes better care of homes, because they are planning to purchase the home."*

Objection #2 – What if you don't pay my mortgage payment? I am not sure that I like the idea of you making my mortgage payment.

There are several ways you can answer this one. Use which one is the most comfortable and fitting for your situation (and true):

Possible Solution A – *I understand your concern. I have been in this business a long time and can give you references from other sellers like yourself if that might make you more comfortable.*

Possible Solution B – *I understand your concern. What would make you more comfortable and yet protect us both?*

If they insist on making the mortgage payment keep in mind in this situation they must then provide proof to you of their payment. You will always want to have bank authorization to check this out yourself. This requires a document that is signed by the seller along with all of the other contracts for the lease option. There should also be authorization in your contracts that if they don't pay on time that you would have the right to change the payments from the seller to the mortgage company. You must protect yourself.

Possible Solution C – *I understand your concern. I could make your payments to the mortgage company and then mail a copy of the receipt to you. This way I am protected and so are you. Would this work for you?*

Objection #2 – Why won't you put more down in the option?

Possible Solution – If I were to put a lot more down, I wouldn't be able to buy more homes, and I'd like to help more sellers just like you. If I put all my money down on your home, then I wouldn't be able to invest in more properties. I am really focused on helping several people right now. Then get a question or something back to them about why they are in their situation – like "You had said you put the home on the market for rent because it didn't sell, right? I want to help you rent it and sell it. You do want to sell right?"

Objection #3 – What if you don't buy?

Possible Solution – Explain to the seller that if you don't purchase the home, then the home reverts to the owner in equal or better condition. Of course you can't just leave someone in the home and give it back to the seller that way – unless all parties agree.

Objection #4 – What happens if you die?

Possible Solution – The contract provisions allow for either if I died or the seller died that the contract still binds our heirs to continue on. It's a good question!

Lease Option Questions the Seller will Ask You

There are a number of other important questions that will come up from the seller as the transaction comes together.

1. **How long does it take for you to buy the home?** – "*Most buyers close between 18 to 24 months.*" Be honest. Because tenant buyers may come and go before one settles in permanently, you need to give yourself time to close the deal, and 18 to 24 months is usually how long it takes for a deal to finalize. We hold the buyer's hand all the way, walk them through the mortgage process and do everything we can to make the purchase occur. We are not, however, mortgage brokers, and offer no mortgage advice. If the first tenant buyer doesn't buy, we need time to be able to find another one (which is why we will want 3-5 years from our sellers).

2. **Why do you need X years to buy this home?** – "*I need time to find the right tenant buyer and get them through the mortgage process.*" Approximately half of my tenants end up exercising, so, it's very important to have enough time to make it work, since with each new tenant at least a year is needed for them to clean up their credit to qualify for a mortgage.

3. **How do I change the insurance on the sales contract**? – *"Call your insurance agent and they will take care of it for you – it just has to be turned into a non-owner-occupied insurance policy."* It doesn't affect the rates much (if any), and in most areas it's about the same rate, but the seller does need to change it so they have the proper insurance. Be willing to even do a 3-way call with the seller and the seller's insurance agent to make sure they get the right coverage.

   They should also put YOU on as an additional insured. Why additional insured? Because **you** have an interest in the property. You will want liability insurance.

   As an additional insured, you also get notice if the policy ever lapses. If their insurance does run out, you have the right to go buy insurance and then bill the seller for it.

4. **What kind of people are going to rent my home?** *"The best kind. I am looking for a future home buyer for your home."* Some sellers want to discriminate regarding the types of tenants that move in, but I have to tell them that by law I can't discriminate. If discrimination issues are important to the seller, I tell them I'm not the right person to sell their home. On the other hand, I'm going to take care of their property and put someone qualified into their home. [Note: There is more information on Fair Housing later on].

5. **What if the tenants trash my home?** Naturally, this is a major concern to any seller. ***"****I can understand this would be a concern of yours, but I want to assure you that I really do screen my tenants carefully. I am not putting just any tenant in your home, I am putting a future home buyer in your home. But if anyone does any*

damage to your home, then I would take care of it. I am fully responsible for your home." If they need further assurance you can let them know that their home is also your investment, so you're looking out for it very carefully.

6. **Can my attorney review the contracts? "***By all means; I recommend it!*"

7. **May I list my home with a Realtor® since you're not ready to commit yet?** "*Absolutely, go ahead and list it but please make sure you list my name as **an exclusion** because if I do buy it during this time period, you don't want to pay a commission on me."*

8. **Can I come look at the property during the lease period?** *"Absolutely, and it says so in the contract, but you need to go through me to do it."* You won't be able to stop by unexpectedly or drop in on the tenants because that would violate the tenant's rights. You'll simply need to call me to coordinate that.

CHAPTER 6

Getting the Paperwork Ready for a Sandwich Lease Option

Now that you've found the motivated seller perfect for a lease option, determined the technique and profitability, and the deal is negotiated, you will next need to get the paperwork ready to be signed by the seller.

For a lease option deal there are different contracts and forms that need to be signed. There are also steps that need to be taken to complete and organize a lease option deal. I use a checklist so that I don't forget any step during the process and can be confident that all items are completed. This is most important when you are new or when you have many properties going at one time. When you are experienced you will know what needs to be done and likely not forget much, however, when you have many properties (like I have had at one time), it becomes more difficult to keep everything straight in your head. Things will potentially slip through the cracks. A checklist is very important to keep things straight on each property.

I have a checklist form for each property. These are reviewed every other day, if not daily, to see if any tasks need to be completed for any of my properties. Nothing gets checked off the checklist until it is completed.

Let's look at the list below and then I will explain each item in more detail. This is the checklist I use:

Buying On An Option - Check List

Address: ________________________

Contact:_________________________

Phone: ________________________

Projected Starting Date:___________

- ☐ Create Owner Folder for this home
- ☐ Order pre-title work
- ☐ Check IRS/State tax liens
- ☐ Check if mortgage is up to date
- ☐ Check if property taxes are paid
- ☐ Draft all documents:
    - ☐ **Rental Agreement/Lease**
    - ☐ **Sales Agreement**
    - ☐ **Option Agreement**
    - ☐ **Memorandum of Option**
    - ☐ **Affidavit of Liens**
    - ☐ **Bank Authorization**
- ☐ Seller's Disclosure
- ☐ Lead Based Paint Disclosure
- ☐ Get a key or access
- ☐ Get an inspection
- ☐ Advertise the home

- ☐ Set up utilities
- ☐ Water Reading (if city H_2O)
- ☐ Water Softener (if house is on a well /if so, is the system rented or owned?)
- ☐ Get insurance (liability)
- ☐ Owner's proof of insurance – additional insured
- ☐ Review title work
- ☐ Sign all documents
- ☐ *Record* Memorandum of Option
- ☐ Set up auto-payments if paying mortgage payment
- ☐ Maintenance/Work to be completed (list work that needs to be done)

____

If you have several properties, keep them filed in order of which ones are projected to start first. These are the ones where I would focus my attentions first. I would also advertise them more heavily.

Fill out the information at the top of the checklist. The address of the property, owner(s) name and phone numbers (how you will reach them – if there are multiple numbers, put them all down), and when the option is projected to start.

1. **Create an Owner Folder for this home -** This is the left-tabbed green folder (think green for money!). I call this the *Owner Folder*. I set one up for each property I buy on an option, outright, subject to, etc. We will use right-tabbed red folders when we sell on an option later – to hold all of the tenant buyer information.

   All of your contracts, memos, notes, surveys, title work, or anything regarding the home will go into this folder. This is strictly for the information with the seller and you now. Nothing from you or the tenant buyer will go into this folder. [Note: Just the tab part or the address is in red or green – not the folder]

2. **Order pre-title work** – This can also be called a "commitment for title". It is not to be confused with title insurance. You cannot get title insurance on property you don't own, but you do want to do any title research to see what, if anything, is on the title and if there are liens on the property. If you order it from a title company or an attorney, it should only take 7-10 days, maybe less if you have a relationship with them. You can also do it yourself if you are knowledgeable in your own state and county about what you need to research and where to research.

   This is where you will make sure with a title company that the title is clear of judgments and liens. Not only check the title liens but the state and IRS tax liens that might go against the person on title. If I go down to my county courthouse to research John Jones on 123 Anystreet, I might only find a mortgage on title, because IRS information is kept at a separate location. However, a title company will pull the information from all relevant sources to give you a complete picture. If there are liens other than the seller's mortgage, this would indicate the seller is not a good candidate for a lease option, but rather a subject-to deal, because this would be considered bad debt on the property.

Also, the title work would show all the owners of the property. It is very important to purchase the property from ALL owners of the property. There are times when I have looked at the title work and seen "Joe and Sally" on the title when Joe had said he owned the property. Joe forgot to mention that he divorced Sally. The problem with this situation is that Sally is still on the deed/title of the home. Sally either has to get off title by deeding her interest to Joe or agree to all the terms of the lease option and sign the paperwork. Whoever is on deed/title ***must all sign***.

I also recommend that married people have their spouse sign documents too. In many states a married man must have his wife sign the deed in order to transfer title, even if she is not on the title, because of her dower rights. I recommend that anyone who is married have their spouse sign my agreements.

3. **Check IRS/State tax liens** – Usually the pre-title work will show both of these, but if you are doing your own research make sure you check for both of these areas and ask the county and someone to help you confirm that the seller does not have any IRS or state tax liens against them. This was covered in #2, but I want to make this abundantly clear if you are doing your own investigating.

4. **Check if the mortgage is up to date** – The best information source for the mortgage is the seller. Many mortgage companies will give their seller a statement each month to show what has been paid, what is still owed, and if any payments are behind. If the seller does not have one, they will have to order a current account statement. If taxes and insurance are escrowed in their monthly payment, then you will also know that those are current. A mortgage company would not let those go unpaid or be delinquent. An escrowed payment is a payment that includes the taxes and insurance as part of the monthly payment.

5. **Check if property taxes are paid -** You can call your local county or state office where taxes are paid and get proof that taxes are current. Find out in your state or area how to confirm that ALL property taxes are current on a home. Call your local city assessor's office and ask them about the home. In some states any back taxes might be paid by the county and the city might not know if the taxes are paid are not, so confirm with the assessor and possibly other real estate investors in your area how you will know if they are up-to-date and paid. You can also ask the seller to provide proof to you of a recent paid tax bill; however, that does not always mean that a tax bill from 2 years ago was paid. Find out and protect yourself.

6. **Draft all the documents** – the documents I listed above in the **Buying on Options Checklist.** There is a copy of each document on my **Buying on Options on-line course.**

Three Main Contracts for a Lease Option

To make a lease option work, three main agreements are needed. It is possible to roll all three into one or two contracts, but I like to keep all three separate to make it clean and clear. It is most important to keep them separate when you sell on an option (explained in that chapter).

- **The Option Agreement** – On the selling side, the option agreement turns control of the property over to the optionee (you) without ownership. When I am doing a lease option, I sign an option with the seller and they give me control for a specified amount of time (usually 2-5 years) during which I will be trying to secure a tenant buyer for their home.

- **The Rental Agreement** - The rental agreement specifies how long I will rent their home and how much I will pay each month for the rental of their home. The rental payment will always go first to their mortgage company if any mortgage is due on the home, then to the owner if any rent is remaining. Examples: If my rent is $1,200 per month and the mortgage payment is $1,300, then the mortgage company will get $1,200 from me and $100 from the owner. If the mortgage payment is $1,200 then the mortgage company will get one check from me for $1,200. If the mortgage payment is $1,100 then I will write one check to the mortgage company for $1,100 and one to the seller for $100.

  The check to the mortgage company needs to always have the mortgage account number on the check so that it gets applied to the correct mortgage. The owner could have two mortgages with the same mortgage company. You really want to protect this mortgage and make sure that this mortgage is getting paid; therefore, put the account number on the memo part of the check.

- **The Sales Contract** – This agreement sets the terms of the final sale. Again, there are two of these – one for my deal with the seller and one for my deal with the tenant buyer. The deal with the seller has a set sale price – and that price remains constant regardless of appreciation or even depreciation. However it is always negotiable up front – i.e. – it could be set that the price is $150,000 if purchased within 2 years and $155,000 if purchased between years 2 and 5. On the tenant side, the contract also has a solid number, and because you set the terms of the lease option, that price will be higher than the price you have with the seller.

Additional Forms For the Seller

There are other forms that the seller will need to sign. They are:

- **Memorandum of Option** - This is the document that gets recorded against the title of the property. It does two things:
  1) It gives the world notice that you have an interest in the property. It does what is called *clouding the title*. When you cloud a title, the seller can't refinance the home or sell the home to someone else and give clear title. A reputable title insurance company would not insure it with this memorandum on the title. It protects your interests in the property and is **VERY important that it gets recorded**. Having it

signed and notarized does you no good. ***Recording*** it is a necessary step.

2) It can *season the title*. Seasoning is a term that is becoming more and more important to real estate investors. Mortgage underwriters are the ones that approve mortgages, and are now becoming very strict on the length of time investors or sellers have owned properties before selling them. There has been so much mortgage fraud in the past few years that the mortgage industry is really cracking down on this. One way to prevent this type of fraud is to make sure that the seller of a home has owned it in their name for 90, 120, even 360 days. Each lender has their own requirements for the number of days to season a title of a property. This becomes important for this strategy (lease option), as a lease option is not ownership. You will be selling a home later that you did not own, but maybe for one hour or so. This can cause a situation for you that needs another solution. There are always solutions to almost any roadblock.

- **Affidavit of Liens -** This is a sworn statement that the seller signs disclosing all of the liens they have on the home. The mortgage should be the only lien; however, this is the sworn statement disclosing this. Also, it asks about liens that are not yet recorded but known about; for example, the roof was done last month, but the roofer was not paid yet, this could become a lien, or maybe they know it will be a lien. They must disclose it, or it would be considered fraud.
- **Bank Authorization -** This document is used to give you authorization to get information on the mortgage. You can find out at any time the status of the mortgage, balance, payment history, payoff amount, etc. It gives you authority to find out information with the mortgage company as if it was your mortgage. *All payments made in the future should be made directly to the mortgage company and not to the seller*. This is why you will want access to the seller's mortgage information. This will protect you from having this home go into foreclosure.
- **Sellers Disclosure -** A statement that is filled out that discloses the condition of the home. The seller must disclose any problems with the home. Each state has a different seller's disclosure statement. Ask a local Realtor® for a blank seller's disclosure statement for your state.
- **Lead Based Paint Disclosure**- Don't overlook this one because it seems obvious. It is a *federal requirement* on the sale or rental of any home. Prior to 1978 there was lead used in some paint products used in residential homes.

  Lead poisoning has caused many problems for people, but primarily permanent damage to children. Because of these problems with lead based paints, HUD has passed a law that requires sellers and landlords to have the lead based paint disclosure signed and the pamphlet called "Protect Your Family From Lead in Your Home" to be given to all buyers and all tenants. If this is not completed, the fines are significant. Don't miss this step!

Also, if you do have lead based paint in your home but you didn't do this step and there is a problem discovered later, imagine how much the jury will hate you if a child is found to have brain damage from your negligence. The jury will give the child's family a judgment award, which will take every dime you ever had, or will have.

Check out your states lead abatement requirements. Some states do require to you completely remove the lead based paint from your rental homes. You may want to avoid those homes or confirm it has been completed prior to you taking it over.

7. **Get a key to the house** – You want to make sure that you have a key or accessibility to the home. If the home is listed through a Realtor®, you may be able to get the lockbox combination and have access to show the home any time if it is vacant. If the seller is still living in the home, which is often the case for me, then I want to make sure that I either have the ability to call the seller when I have a showing and/or that the seller gives me a key and I call them when I am going to be showing it. If the seller will give you a key, you will want to consider a lockbox. You can purchase these at most hardware stores.

8. **Advertise the house** – Get the home advertised as soon as you know it has passed your inspection, perhaps even before (remember my Stupidest Move Award—you don't want it sitting vacant!). You really want your time of vacancy to be minimal. Get it in the newspaper, with local employers, on a website, etc. Advertise anywhere you can find a buyer.

9. **Set up the utilities** – Do this when you are actually going to be taking possession of the property or the time frame is actually starting for taking possession of the property. For example, if it's April 28, and I'm taking the property on May 1, I want to go ahead and turn on the utilities in my name. This is the electrical, water, gas, etc. You will want to turn on anything that is required to be in your name and out of the seller's name.

   Be especially careful for winter months in cold parts of the country. You will not want any days to go by without heat. I have had ice skating rinks in a few of my homes over the years because the heat was not turned on. See why I do my checklists? ☺

   - **Water Reading**: You also want to do a final water reading. In some cities and municipalities, water can be a lien against the home if not paid, so you want to make sure it's current and paid from the day that you take possession from the seller. Also, have the water bill mailed directly to you. This way you can pay it and bill the tenant or you can bill the tenant and know that it is getting paid. You do not want a lien to accrue on the home.

   - **Water Softener**: If there is a water softener on the property, you want to make sure you are taking care of that. If it's a rented softener unit, you want to make sure you turn that contract into your name. I have a water softener company that I work with, and I will set up a lease to own on the softener equipment. The tenant actually pays the bill, and if the tenant(s) end up not exercising, then at the end of their lease the water softener belongs to me. Having a water softener is critical if you have hard water. If you have city water, most likely you will not need a water softener.

10. **Get Liability Insurance** – You're not going to insure the property itself, but you'll want to carry liability insurance that will cover you for doing these types of transactions. Since you don't own the home, you can't actually insure the home. However, you have a liability issue just by being the landlord of the home. As far as the tenant is concerned, YOU are the landlord, and as far as the owner is concerned, YOU are the tenant. You have both tenant and landlord "roles" when you don't even own the property, so I recommend some type of commercial general liability policy that would cover you for properties you don't own.

    This is not going to be a make or break on your first deal or two, but something you will need to consider for this business. Talk to an insurance agent to get educated, but do get several opinions and quotes. Some will try to over-insure you and sell you more insurance than you need.

11. **Owners Proof of Insurance** – Make sure the owner has insurance on the home itself. If they have a mortgage, the mortgage company will require it, but if they own it free and clear, they may not have insurance. You will also want to make sure that they name you as an additional insured on the insurance policy. Some insurance companies will not want to put you on their policy without you being an actual lien holder (like a mortgage holder- see the advanced strategies chapter for an idea here).

    My **rental agreement** and my **sales agreement** require my owner to put me as an additional insured on their homeowner's policy. They might have to switch insurance companies to find an insurance company that will do this. There are several benefits when being an additional insured:
    1) You do get liability protection
    2) You should get notified if the seller cancels their insurance policy for any reason, even non-payment, and

Wendy's Tip

I always recommend having a witness when you are signing a document, but a witness is not necessary to make it valid.

Only the memorandum of option needs to be notarized so that it can be recorded.

    3) You probably will be on any settlement check if the home burned down. Being an additional insured is a great thing, but should not usually be a deal breaker.

12. **Review the title work when it comes back** – Check for liens and for ownership. Make sure it's clean and clear from what you were expecting. You will want no surprises. Do understand, however, that there are things that do show up on the title work that can be an error. I have had several show up with old mortgages on them, but you won't know until you ask the owner. It appears as if the owner has two mortgages. Don't assume they didn't tell you or that they are hiding something, ask them about the mortgages showing on the title work. Many times the owner had refinanced the home and the old mortgage didn't get discharged properly. Don't be alarmed, just get the old one cleared up. The title company can help you with all of this.

13. **Make sure all of the documents are signed by the seller and you** – Have 2 complete, signed sets: one for them and one for you.

14. **Record the Memorandum of Option** – This document is usually recorded at the county office. Once you are certain that you are going to move forward with the deal, if you've got a start date coming up or if you've got a buyer in the property, then you want to record the memorandum of option. This will get recorded against the title – it shows the world that you have a claim against the property and that you have the right to buy it on an option. This document is filed at the county where the seller's home resides, or wherever you record a deed.

Wendy's Tip

Make certain that you leave a 2.5" blank margin at the top of your memorandum of option or it will not be able to be recorded! Check your state/county recording requirements prior to completion of this form.

15. **Set up the payments with the seller** – You can set up an automatic payment with the Mortgage Company that goes directly out of your bank account. I use QuickBooks and it will set up automatic payments so that you don't forget to write the checks out in a timely fashion.

Wendy's Tip

When juggling the receiving of the rent from the tenant and the payment of the mortgage to the owner, you might want to stagger them a few days to give the tenant's payment time to clear before you make a payment to the owner.

16. A list of maintenance or work to be completed before I take possession – This is a list that either you or the seller are responsible for, depending on what deal you have made with the seller (e.g., replace linoleum, repaint trim, replace mailbox). All repairs are to be done by my contractors (so I can control the quality) unless otherwise specified. All repairs, both major and minor, are the responsibility of the tenant except for the first 60 days of the agreement – I leave that responsibility to the owner. For instance, if the furnace were to go out two days after I took possession, I don't want to be responsible for that. Now, everything is negotiable; 60 days is just my standard. You can make it longer, you can make the seller responsible for all repairs, for anything over/under $500, nothing at all, etc.

Some of My Favorite Clauses for the Three Main Lease Option Contracts

In each state you may have required information for your rental agreements and purchase agreements. I offer contracts on my website that are generic and can be used in all states, but your contracts should always be checked by a local attorney as each state has its own unique laws.

Therefore, you should to get the advice of an attorney. Attorneys can be very expensive; therefore, I recommend some of the best attorneys – and most reasonable – through Pre-Paid Legal Services. You can find out more at www.Prepaidlegal.com/hub/Wendypatton, but as a quick introduction, it offers plans at very reasonable monthly rates that give you legal assistance. I have been a customer since 1997 and have saved thousands of dollars on legal questions, contract reviews, letters, etc. for real estate matters and in multiple states.

Each state has its own rules and regulations regarding rentals, lead based paint abatement, evictions, etc. Here are some of the clauses that have been my favorite over the years in my contracts to buy on lease options. Depending on what you have negotiated with your seller, you may want to use these clauses, and they may or may not always apply. They are just some examples of things I have used with my sellers:

The Option Agreement

- There shall be an additional option consideration of $_____ per month given by Optionor to Optionee as credit towards purchasing the home.
- Optionee has the right to multiple-list, advertise, or resale this property before or during the option period.
- Should the property become uninhabitable at any point during the lease period the tenant will be released from all rent liabilities until the property is habitable and is re-let. The amount of time that the home is uninhabitable will be the time period that will be added to the option agreement and attached rental agreement and offer to purchase.

The Rental Agreement (Lease)

- Tenant will have access to the home on ____ to show the property to prospective tenant/buyers and contractors.
- Tenant will be assigning this agreement to anther party, but is still responsible to the owner per this agreement

- The owner gives the tenant the right to make repairs/improvements to the property at the tenant's expense. All repairs and improvements will be done with the tenant's contractors.
- Landlord agrees to use his/her homeowner's insurance to cover any items/repairs/damage that would be covered under their policy (i.e. storm damage, fire, etc) – since tenant can't utilize their insurance for these types of repairs.

The Sales Contract

- Purchaser will put $_____ down on this property. Check will be written directly to: Realty company of listing office upon execution of the attached rental agreement. This amount will be applied directly to the purchase price at closing, and any listing commission owing. The remaining commission, if any, will be paid at closing out of seller's proceeds to the appropriate offices.
- Seller agrees to change his/her homeowners insurance policy to a non-owner-occupied policy and to name the purchaser as an additional insured within 3 days of purchaser taking possession of the home.

The paperwork is vital to your successful ability to make a lease option deal, so don't skip any steps, and make sure all areas of the checklist are covered. You will add your own favorites over the years that you do lease options and learn new ideas.

CHAPTER 7

Advanced Concepts and Strategies for Buying on Lease Options

I have suggested strategies that you should initially start with, but there are more advanced strategies that can also be considered for lease options that will build your portfolio to greater depths. When I started out, I used only basic strategies; however, over the years there have been some things that I have learned from other students and national speakers that helped me take my deals to another level.

These strategies are not essential, but they can certainly sweeten your overall profit or afford you greater protection. You will need to evaluate each situation on its merits, and remember that all of your strategies must be negotiated before any paperwork is signed. Sometimes these techniques can scare some sellers away. They can be too complex or seem too difficult, therefore you will need to know your seller and understand them by building that relationship.

Extra Ways to Protect Yourself on a Lease Option

There are some things you can do in the area of lease options that will give you the extra protection of not being the title holder. Besides filing a memorandum of option described in Chapter 6, here are some additional strategies:

1) **Place a deed in escrow** – The seller would actually sign the deed when they sign all of the lease option contracts; however, the deed does not get recorded on the title. It gets held by an attorney or title company, in most cases, with instructions on when the deed can be released and recorded. This does not protect the title against liens being filed against it, but it does in many cases allow for the investor to close on the home without the seller present.

   When the title is held it will also include instructions on how and when it can be released – for example: *When Wendy Patton pays $155,000 in certified funds to Joe Smith, this deed can be released to her. These funds must be paid by XX/XX/XXXX.*

   Although placing the deed in escrow does not keep the title protected, it does give most sellers the feeling that they have 'deeded' or sold their property. I think sellers are much less likely to try to back out later on a lease option deal when they have signed a deed and placed it in escrow.

2) **Performance Mortgage** – A performance mortgage is used for several reasons that will protect you. A performance mortgage is like any mortgage except that it is for the performance of the seller to sell their home to you. It is a mortgage on

their home that they grant to you. I think they are a very good concept; however, I have found that many sellers find signing them objectionable, therefore, you will need to utilize this one only when appropriate and where it can be accomplished with the seller. These are fairly complex and I don't use them—I just want you to know they exist.

3. **Limited Power of Attorney**

There are many states where the transfer fees (the costs to record a deed) are extremely high and doing a simultaneous closing (discussed in detail in Chapter 13) becomes expensive. Some states' fees are up to 3% of the sales price of the home. On a home priced at $400,000 this would take an extra $12,000 in profit right off the top of each deal for investors in those states. There are two ways around this:

Option 1: You can have the seller sign a new purchase agreement with your tenant buyer for the new amount and you pay the difference in fees for what you paid the seller vs. what you sold it to for your buyer – e.g., you paid $350,000 to the seller and you sold it for $400,000 – you would have the seller sign a new contact with your tenant buyer for the $400,000 and you pay the extra costs on the additional $50,000 raised price.

This is fine if you don't mind and the seller doesn't mind the entire deal being laid out in front of them. Sometimes this is no big deal, other times it causes bad feelings. The sellers always know you are making a profit, but to put it in front of their faces can rob their job of the deal that once was a win/win for them. You will have to decide if this will work for your seller. Only you know your seller and how they will feel about the deal if you did it this way at the end.

To appease the seller, you also can offer to give them a little 'bonus' with this. For instance, let's say they were going to receive $95,000 in cash at closing, if they sign this document, now you will give them $96,000 at closing. It now becomes more of a win/win. They get more money and so do you. You only pay $1,000 for the first $250,000 in closing cost and then your state's regular rates on the additional $50,000 on the raised price.

Option 2: You decide you don't want the seller to see the details or they are out of state anyway. You can have the seller fill out a limited power of attorney. This would allow you to sign documents on their behalf for this home at closing. You can then change the price to the new price, and sign on their behalf. It is completely legal and legitimate as long as they get the amount they were supposed to receive at closing. They will have to have a payoff letter prior to closing for the title company or attorney. It might have to have dollar figure of payoff vs. the sales price. It might say something like this:

To Whom It May Concern:

I am to receive $XXXX in my closing with Wendy Patton (and you subtract the closing costs and figure out what they should receive and type the letter for them so it is ready and sent to you or the attorney/title company). Please mail my check to __________. Call me for any questions at (111)222-3333. I will not be at closing, but Wendy will be signing the documents on my behalf, for which I have signed a limited power of attorney.

Sincerely,

Joe Smith

Here is what a limited power of attorney may look like.

LIMITED POWER OF ATTORNEY

This limited Power of Attorney is given to Wendy Patton , for the purpose of Closing, Closing Documents, Contract Changes that don't affect owner's bottom line, Insurance, Mortgage Payments, etc., or any other matters that pertain to the property located at:

____

This limited Power of Attorney shall become valid as of the date signed below and be in force until the final closing of the property. Photocopies of this document shall herby be treated as original counterparts.

POWER OF ATTORNEY GIVEN TO: **Wendy Patton - or your name ☺**

Agreed to by:

______________________________	______________________________
Seller's Name	Seller's Name
______________________________	______________________________
Date	Date

NOTARY

STATE OF COUNTY OF __________________

Before me personally appeared ____________________ ____________________________

To me well known and known to me to be the person described in and who executed the foregoing instrument, and acknowledged to and before me that he executed said instrument for the purposes therein expressed. WITNESS my hand and official seal in the State and County aforesaid, this ______________ day of ________________ 20XX.

____

Notary Public Signed

______________________ ______________________

My County of Residence My Commission Expires

4. **Partner with the Seller for High-End or Hot Markets -** There are some states and locations where property values are very high and might be cost prohibitive or risky.

   Consider partnering on those homes with the seller -- that is, inviting the seller to become a partner in the profit of the sale. If a home is worth $700,000 and the rental rate is $3,000.00 per month, you may have reservations about taking on this type of property; however, this home may also net $150,000 or more in profit.

   A seller of this home may also feel uncomfortable giving away all the profit for this type of property. This might become an objection for a seller in this price range or in a hot market that is appreciating rapidly. It is often wise to offer to partner with this type of seller.

   Partnerships don't always mean 50/50; it's up to you to determine what's fair in each situation. If you are doing all the work, they should cover all the risks. For instance, if the home is vacant, the seller should continue to cover the monthly mortgage payment, or if the tenant buyer doesn't pay their rent, then the seller should cover the payment. If they want part of the reward, they need to cover the risk.

5. **Land development -**I love land development. Land development is extremely profitable in areas of the country where land is valuable. For instance, in my area of Michigan, even a very small lot used to sell for $40,000, but not as much now that the market has gone down. If I can buy just a house valued at $150,000 that might have a bigger lot then normal, I can then split that lot and add $40,000 to the value. It will not affect the value of the home much if the surrounding homes sit on the same size of property, but it makes that house and lot combination worth more for me, the investor.

   This can be even more profitably when the home needs renovation or can be lease optioned out to a new buyer for more than the original $150,000. You can do something mid-size like an eight-acre parcel and do five one-acre home sites, depending on your zoning requirements.

Ethics and Capital Gains

One area of Ethics to be aware of – Capital Gains for Sellers on Lease Options

There are ethical issues you will need to deal with in the real estate investing business. Many times we will know about certain IRS or other regulations or laws relating to real estate that the seller may not understand or even consider when making a deal with us. It is important to deal with everyone fairly. The rules with the IRS are constantly changing and you can't give tax advice unless you are a CPA - so have the seller check with their CPA or tax advisor - but you should be aware of the capital gains rules and how they can affect your sellers.

The Capital Gains Rule

(check with a tax advisor as this can change at any time)

If you have lived in the property as your primary residence for more than two years and you sell it, you don't have to pay capital gains. The IRS has changed the capital gains on our personal residences to a rule that in simplified terms goes like this: Every two years you can sell your primary residence (yes, the one you LIVE in -- not your investment deals!) and you can keep the profits of up to $250,000 if you are single and $500,000 if you are married tax free.

Wendy's Ethics Example – Capital Gains

Suppose you have an older woman who has lived in a house for 30 years and she's got over $200,000 worth of capital gains. The IRS allows you to have up to $250,000 capital gains tax-free if you are an individual and $500,000 if you are a couple. If you buy her house within 3 years, she pays no capital gains, but if you go over that even by one day, she'll have to pay taxes on the $200,000 in capital gains. Your inability to close a deal within the three year period could cost her tens of thousands of dollars, and that's just not fair to her.

If you have done a five year option with her, you have just erased the most recent two years she has lived in the home and potentially exposed her to capital gains. Many sellers think the law of "One sell time over age 55 and no capital gains" still exists but it doesn't, and it is your responsibility to educate both yourself and the seller about pertinent changes in the law.

I care about the people that have been in their homes many years and who have a lot of capital gain – and therefore a lot to lose – especially since they probably don't understand the current tax laws. If your seller has a lot of capital gains, advise them to speak with their CPA and attorney if they really want to go for a five-year deal so that they understand the financial risks and liabilities.

Anything above that is taxable, and any time period different than that becomes more complex. Basically, if the seller lives in it for 2 out of 5 years, it qualifies for this tax free gain. This allows the seller to rent this home for 3 years, but not one day longer.

However, if I know the seller has little to no equity in the home, I am far less concerned about their capital gains and may do a 5-year option.

What to do when your option has come to an end…

Time is out on your contract – now what? Let's assume you had three years with the seller to purchase their home. That time is fast approaching and you have no buyer that can purchase yet. First make sure you don't end a contract with a potential buyer on the same day as your contract ends with the seller. I recommended leaving three to six months at the back end of a deal. For instance, if you have three years with the seller, you give your buyer 18 months. If they don't exercise, then give the next tenant buyer only 12 months, therefore, leaving yourself six months at the end of your contact with the seller for other plans. Let's say buyer number two doesn't want to exercise either. What are your choices? Surprisingly, there are many. You can do any of the following and in any order you choose, but I recommend to always try number one first:

1. ***Ask the seller for an extension (if you want one) --*** Most sellers will give you an extension if you ask. Many times the sellers will just give it to you with no costs. Sometimes the extension might cost you more money -- a little more now, in the future on the sales price, or on monthly payments. If you work it out for a win/win then do it. Make sure the extension is in writing. Don't take their word for it. All real estate deals MUST be in writing or they are not enforceable.

2. ***Buy it yourself*** **--**You can get a mortgage with a lender and purchase the home. You would definitely want to consider this if you can afford to do it and there is enough profit in the deal. Don't give the home back to the seller unless it is not worth the amount you agreed upon or there is something wrong with the market or the home (that you didn't create with yourself or your tenant). With 12 months of cancelled checks on a lease option, you can usually get a mortgage that is treated like a refinance vs. a purchase. This type of program is also available to your buyers after 12 months of payments. If your mortgage broker doesn't have this program, find another mortgage broker (however the mortgage industry is always a moving target also). You don't always need good credit yourself if there is enough equity. Look around and talk to some lenders, but don't wait until thirty days before the end, talk to them months in advance. Sometimes these types of loans can take months. I found this out the hard way.

3. ***Sell the home directly to another buyer*** **--**You will have to sell the home to another buyer directly. It will just not be a tenant buyer. It will be someone from a Realtor® or someone you found in the newspaper. You can sell it to anyone you would like.

4. ***Partner with someone if you can't do the mortgage yourself*** -- If the home has some equity and you can't refinance it, you can't sell it, and the seller won't extend, then bring in a money partner who can get the mortgage. Give them a part of the equity or a fixed amount

for doing the financing. This will give you more time to resell it on the market or to lease option it again. You can find money partners all day long in your local real estate investing group.

5. ***Don't exercise your option --***Tell the seller you don't want to purchase and then you can walk away from the deal. Remember that an option with the seller only gives you the right, not the obligation, to purchase. You must return the home in equal or better condition, less any normal wear and tear. You can't return the home with damage.

6. ***Assign the deal to another investor --*** You can wholesale this lease option to another investor for a fee, then they can do one of the above five choices.

CHAPTER 8

Building Rapport and Sharing Lease Options with Realtors

Why Work with Realtors?

Realtors® have 80-90% of the nice homes listed on the market. It varies from city to city and area to area, but they certainly control most of the market that is for sale. They have the sellers that I need to get to in order to buy those homes.

Working with Realtors® will change your investment strategy forever. Now deals come to me easily. Honestly, I get more deals than I can go look at. I don't chase them anymore. Once you get the "Realtor® System" working for you, you will only need to evaluate which deals you want to pursue. The "Realtor® System" will get Realtors® bringing you deals.

Many investors think real estate agents don't have the best deals or that they have been picked over by the time they actually hit the market. In many cases, this is true. There are deals that don't hit the market because they are very good. Realtors® have clients that buy the best deals before they ever list them on the MLS (Multiple Listing Service). There are also deals that never get to a Realtor®, because the seller doesn't ever list them with a Realtor® – e.g. foreclosures, traditional for sale by owners, the homes investors find by driving by, etc. - but I believe some of the sweetest deals are sitting on the market listed with a Realtor®. It is true that some of the best deals get snatched up before they hit the market, but there are many other deals left behind that no one even sees. The reason that no one sees them is because they are looking for traditional or wholesale type of investments homes, meaning paying cash or getting a mortgage on the home, and not lease option homes.

When an investor considers traditional financing or paying with cash, they must be able to buy the home for a much better price. However, when they can buy the home on a lease option (terms) then they can pay a higher price, therefore opening up the market to more properties to choose from. When working with Realtors®, it is less likely to be able to "lowball" a home and get the deal through. Realtors® don't typically like investors for that reason.

Since most of my lease option deals come from Realtors®, it is important to first understand the perspective of most Realtors®. Most Realtors® are trained to sell real estate for a living – traditionally. They are taught to sell real estate traditionally from beginning to end in these ways:

Steps a Realtor® Goes through on a Traditional Sale

1st
- List a Home for Sale

2nd
- Find a Buyer

3rd
- Get a Contract Signed

4th
- Have the Buyer Get a Mortgage

5th
- Close on the Home

6th
- Get their Commission!

Most of Realtor® deals are done in the above traditional way, but what about the times when their listings don't sell or they don't sell quickly enough for the seller to feel comfortable? Realtors® are not taught to bring creative alternatives to the table for their sellers. That's where I come in. I teach them about the alternatives I offer and how I can help them help their seller.

How the Market Affects Realtors®

In a strong seller's market, Realtors® typically don't need to consider anything creative, because homes are selling very quickly. However, even in a seller's market there are some homes that won't sell quickly for some reason. These are the homes that Realtors® will need to consider being creative with.

When you are in a buyer's market it is much easier to work with Realtors® as well as sellers on creative ideas, as they will to be more open to ways to sell their listings. In a buyer's market the Realtors® won't get any commission if the home doesn't sell or if the listing expires, and the seller lists the home with another Realtor®. Also, in a buyer's market, sellers tend to put more pressure on their Realtors® to sell their home. This pushes the Realtor® to be more open-minded to new ideas and to pursue other alternatives for their sellers. They really do want to sell their customers' homes. This helps their sellers and their own business. That's where I come in. I teach them about the alternatives I offer and how I can help them help their seller.

Finding the Right Realtor®

The Realtor® you will need to find for lease options will be a seller's agent or what is called a *listing agent*, the one that lists the home for a seller. A listing agent is the one who works with the seller and has his or her name rider on a sign in someone's yard. If you want to buy in a certain neighborhood, you can usually find the strong listing agents by driving through and seeing whose names appear on the real estate signs in the yards.

The buyer's agent is one that represents and works for the buyer. A buyer's agent looks out for the best interests of the buyer whereas a seller's agent (listing agent) looks out for the best interest of the seller. A buyer's agent is whom you would select to look for and purchase your own home. A listing agent is whom you'd want to work with when buying lease options or lease purchases – with my strategy.

Realtors® have a relationship with their seller that is very unique. Sellers tell their Realtors almost everything about their personal lives. Realtors therefore know who is motivated and why. They know who is getting divorced, if they are in trouble financially, if their builder is almost done with their new home, if they have custody issues, if they are getting worried about double house payments, how many grandchildren they have, the name of their dog who died last year, what Uncle Ned did at the last family reunion, and the list goes on. Sometimes it's a case of enormous volume they're telling you and the little bit you actually need to know. I am sure Realtors® want to say, "That's really more about your personal life than I ever wanted to know." But they never say it. As a Realtor®, I am sure they would just stay as interested as possible in order to build rapport.

Because the Realtor® is providing a very needed service to the homeowner – that of helping them to sell their house, and because the homeowner so freely tells the agent *everything*, the homeowner is not shy about calling up and saying the *four letter word* after the home has been sitting on the market a while. "Realtor®, if you don't sell my home soon, I am going to have to RENT it!" **R-E-N-T is that dreaded 4-letter word**. When a seller says that to a Realtor®, a Realtor® will cringe. It is the worst thing you can say to a Realtor®, other than, "Take my home off the market." If the home doesn't sell soon the Realtor® won't get any commission and has lost countless hours in showing the home as well as dollars in advertising and marketing. That's a scary thing! Although, the Realtor® can rent it for the seller, and is licensed to rent it, most Realtors® don't know how or don't want to rent it. The commission is so small to rent a home, it is generally not worth their time unless they are a property management company and do a large volume of rentals. Many real estate companies really don't do rental properties at all because it is such a different type of business and carries one of the biggest liabilities for Realtors®.

In my area, when a Realtor® hears the "four letter word" RENT, my phone rings. I have spent years developing rapport with the many real estate offices in my area as well as with individual Realtors®. They know what I am looking for, and they know how to pique my interest in ways that might get me to take a drive by the house and see if I'm interested. Why? Because when they work with me to give me leads on potential lease options, they know they can get their commission paid – and not only paid but paid much more quickly than on a traditional rental deal. Although I don't technically pay their commission - the seller always pays that - I am willing to front the commission. This creates a win/win/win between the Realtor®, seller and me – the Realtor® sells their listing, the seller sells their home, and I buy another investment home. We all win!

Networking with Realtors®

You only need to work with two to four listing agents per year to make a comfortable living. You can find listing agents in the real estate section of your newspaper, through personal contacts or your investor groups. If you have been working with a Realtor® in your area, your phone should ring as soon as the Realtor® hears the four letter word "rent." I have one Realtor® in my area who gives me one deal a year, but I make at least $30,000 off her every year. I stay in touch with her every few months just to keep my name fresh and to keep the relationship moving forward. It's key to find Realtors® that you can work with. It only takes a few Realtors® to keep you going.

Realtors® know lots of other Realtors®. If you have one contact, you can network through that one to access many others. Research when they have local functions and go mingle. You can find where these meetings are by calling the local real estate board. Exchange business cards at the functions. If you don't have business cards, have some printed. It's more important at this point for you to have their cards than for them to have yours, but having a card to exchange is more professional. You want them to know who you are and how to get in contact with you.

Take a Realtor® out to lunch. Rent a conference room and have a wine and cheese party and then give them a presentation about lease options or lease purchases. Give them a "trigger point" that says "Would you like to sell more listings and make more money this year? I can teach you for FREE!" Do something to advertise it that grabs their attention without giving away all the details. Don't be alarmed if only 5-6 people show up because those 5-6 are very interested in creative solutions. You might even put on your invitations: "Would you like to be more creative than your competition? Would you like to know things that your competition doesn't know about yet? I can teach you some creative ways to sell your listings that your competition hasn't even thought of."

If you are not sure who to call, talk to the people in your local investing group since there will be some Realtors® there in your group. These are not the Realtors® you will be working with, as these are investors themselves and not traditional listing agents, but those Realtors® should be able to tell you who the listing agents are in their offices. The top listing agents from the companies are also listed in the paper. It's worth starting a database or spreadsheet to keep up with who is where and what they do – especially of the people you begin to contact and develop relationships with. And, of course, keep a backup copy of your information somewhere and back up your data regularly. It won't take many good listing agents to make this business lucrative for you.

Your local investors group can also be a great resource from brainstorming on how to get more ideas on drawing people in. Not only will they be interested in giving you feedback, you may even find a money or managing partner there who is also keen on investing in the lease option strategy. You can then go in as a team and make a presentation.

Sharing the "Realtor® System" and Targeting Realtors®

Just as you need to build rapport with your sellers, you also need to build rapport and credibility with Realtors®. Working the Realtor® system is a multi-step process. Building a relationship with a Realtor® does not happen overnight, just like with any other good relationship. Here are some steps to get the process moving forward:

I use several tools and techniques to target Realtors® to call me about lease options and lease purchases. I use primarily letters, phone calls and presentations.

Letters: I have a couple of letters that I use to target Realtors®. I primarily target homes listed over 90 days on the market. One letter is for use during a buyer's market (lease options) and the other for use during a seller's market (lease purchase). They both explain when a Realtor® should consider me, and how lease options and lease purchases can help them and their sellers. It is VERY important that a Realtor® understands how you will help their seller. Their first obligation, by contract, is to their seller. Then they are concerned about themselves. My letter explains how I will help their seller AND pay them.

Phone Calls: I will also call Realtors® and go over something similar to what my letter says. You might want to catch them after hours so you can get your entire thoughts out on their voice mail and not flub it up, or if your time is limited. Then they can listen to it over and over and call you back for any questions. Also, it doesn't tie you up for a 30-minute call if there is no interest. However, if you have time when you are first starting out, it might be wise to call during the day. For me, I am very busy now and don't have the extra time during the day for those calls, so I would prefer to get out what I want to say and be done with the call.

Basically I will say something like this, "Hi Sally, this is Wendy Patton from Keller Williams. I am calling about your listing on 123 XYZ Street. I am wondering if it was still available? [Small pause] I noticed it has been on the market for a while and I wonder if your sellers would consider something a little creative? Something like a lease option? If your sellers don't need their cash out now but would like their monthly payment made and you would like to sell their home and get paid your full commission, please give me a call. Sally, if it won't work for this seller, but if any of your other sellers have said to you that if their home doesn't sell soon, they might have to consider renting it, please give me a call. I buy homes when sellers can consider terms like this. Don't lose your commission to sellers that want to rent… please call me. Thanks Sally for considering this. My number is… again my number is … and my name is Wendy Patton at Majestic Realty. Thanks Sally."

Now this might be what I would say in a buyer's market. If it was a seller's market I might change the wording to a *lease purchase*. I would say it was a guaranteed sell for the seller and the Realtor's commission is paid upfront. This makes it a much stronger call and necessary in that market. (See Chapter 9 for the letter in the seller's market – verbiage that makes it stronger for the Realtor)

Getting your Foot in the Real Estate Office Door

Real estate offices get many requests to have speakers and sales people, so it can become hard to get an appointment. The best way to start is to first go to a real estate office where they know you and can recommend you. If you know someone who is a Realtor® or investor, ask them if they can assist you in getting onto a company meeting agenda so that you can do your presentation. If you don't have a contact, call the office directly and speak to the office manager, or broker, and use an introductory letter. Tell them a little about yourself, keep it short and sweet and ask if you can present your ideas to their staff. They get bombarded daily with mortgage companies, title companies, and many others trying to get their business, so they don't like a lot of sales people and they like to keep it short and sweet. However, what you have to keep in mind is that the lease option or lease purchase system offers something unique and different. The real key is to show them how this system will help them to sell more of their listings.

I like to send a letter to the broker that grabs their attention. That means I leave out stuff about me, my background and my credentials, because when it comes down to it, I'm trying to sell a concept more than I'm trying to sell me.

Your letter should be on letterhead and might sound something like:

Dear [Broker], (use their name) *Date*

Would you like to assist your agents in learning new ways to sell their listings? I buy real estate and I have some ideas for your agents on how to sell more of their listings. I buy many homes in this area. I have a professional presentation that I would like to show you and your agents. I understand you get bombarded with sales people trying to speak to your agents; I am not a salesperson. What I offer is unique and is something every real estate agent should know about.

I have some creative ideas that might help you sell some of your office listings. I don't sell anything. I would love to meet with you to explain some of my ideas. My presentation is 10-15 minutes, so it will not take up much time, but will be very valuable for your agents and your company.

We have many references from clients like yours and from other real estate agents, including Agent 1, Agent 2, Agent 3, etc. Please talk to them to find out how easy it is to sell a home to [Your Company Name]. Please call me to set up a time when I would be able to meet with you and share the information and presentation that I would like to give to your real estate agents. My phone number is (222)333-2222.

Sincerely,

Wendy Patton

I also have letters that target specific Realtors® and their listings, and I send them out constantly.

"Educating" Realtors®

Realtors® are not trained to do creative selling, and sometimes investors think they are not too sharp because they don't know how to do unique deals - that's the biggest problem for investors to work creatively and effectively with Realtors® – investors expect something Realtors® are not trained to do. As an investor, you will need to work with a Realtor® and teach them what you need them to know if you want them to work effectively with you. This doesn't mean exactly how to invest, but what key words they should listen for and how it will help their seller and themselves.

When you get a real estate license, you are trained mostly on the law – seller contracts, lead based paint, legal issues, fair housing, things that are required by the state to make a real estate transaction go professionally from start to finish. However, they don't teach you about "what if the house doesn't sell," or "what if the seller says that 4-letter word?" It will then be your job to train a Realtor® on what to listen for and how to help you and themselves in these types of deals. You essentially will need to train them on how to listen for the "four letter word," not on how to do the mechanics of a lease option.

Most of us know at least one Realtor® or we know someone who knows a Realtor®. You can do a formal or informal presentation on lease options or lease purchases to Realtors®. They can be your first Realtor® to meet with and practice your presentation and ideas on lease options. While you are in the practice mode, ask them for feedback; for example, "Did I present the lease option concept clearly?" "Was my presentation too long? Too short?" "Is there a better way for me to communicate this idea to Realtors®?" "May I set up an appointment to present this at your local office?" The last question is especially good if your practice presentation has gone well and you are ready for the next step.

You will then want to go to the Realtor®'s office meeting. Call their broker or have them set you up to come to one of their meetings.

What to Bring to a Meeting

You must have a presentation prepared before going into a meeting. Don't ever think that you know enough to just wing it. Here's a list of what to bring:

1. When you attend a meeting, it is customary to bring donuts or bagels, so call first and ask the office manager or broker what the agents would like.

2. Have all the material that you need for your presentation organized neatly and accessibly. You don't want to be fumbling for information and making them wait on you. Time is money. They will want you to be in and out quickly.

3. Extra business cards (stapled to your handout).

4. Enough handouts of your presentation for everyone who attends the meeting and for the absentee agents. You'll need to call first and get a head count. Always have more than necessary in case they ask for extra copies. You won't need to give them a copy

of each slide you present, but you can give them a one page overview of how lease options will help them as a Realtor® and their seller.

5. Make sure all handouts have your name and contact number on them.

Begin your presentation

Realtors® are open to the idea of lease options, or lease purchases, if you help them understand how they work and when they are appropriate for their sellers. Lease options are not the right thing for all sellers. This will all be about how to educate them on the benefits to themselves and to their sellers. I have a PowerPoint presentation I give, and I go over the program step by step and then open it up to questions and answers afterwards. Here is an approximation of my presentation. It takes about ten minutes, and yours should take no longer.

If you don't have a computer to bring with a PowerPoint presentation, you can make overhead projector slides.

My Presentation to Realtors®

Your presentation might start off something like this:

"Thank you for allowing me to come to your meeting today (always remember to thank them for their time). *I am here to talk to you about some very exciting concepts that I have discovered that work for Realtors® and their clients. Specifically, creative options for Realtors® – things that you may not have thought about before or may not have considered for your clients. Let's get started."*

1. Introduction of myself and the name of my company
2. My agenda: discuss creative and innovative options for Realtors®
   A. Why I'm not a competitor but a help
   B. How to help them sell their listings
   C. Unconventional vs. traditional
3. What to look for in a seller who might need my services
4. What to look for in a buyer who they can't help
5. The Lease Purchase or Lease Options – when I do it and the guarantee it brings
   A. How it works
   B. How I pay commission
   C. Benefits to the seller
      i. Take over payments
      ii. Take over maintenance
      iii. No rental headaches
   D. Benefits to the listing agent
      i. Quick sale – saves time and money
      ii. Commission paid up-front
6. What types of homes are acceptable to me
7. What price range I'll consider
8. Referral fees
9. Closing statements
10. Ask if they have any questions

I don't stay very long once I'm done. Usually the questions are brief and I'll stay as long as they continue to ask for more information. But Realtors® generally don't have a lot of free time in the office, so they're looking to get as much information from me in as short amount of time as possible. Many times, after my presentation, they realize how I can help their sellers. Then they start to write down addresses on the back of their business cards for me. I walk out of presentations many times with lots of cards and leads to pursue.

Making the Realtor® Part of Your Team

If you're new at this business, you might feel like a very little fish in a big pond, but when you have established a relationship with a Realtor®, they become a part of your team whether they realize it or not. Now you're going to start to work together on finding solutions for the "RENT" problem. You will also be able to help them during a buyer's market when things are slow by cherry-picking their motivated seller deals as investments.

Because they are a part of your team, you will want to build that relationship above and beyond just what they can do for you and what you can do for them. How about sending a thank-you gift every time a deal goes through that they have lead you to? These little rewards go a long way in keeping the rapport top-notch and ensuring even more leads in the future!

Building Rapport: The Follow Up

Follow up monthly with Realtors® who might be strong listing agents or ones that work with lots of sellers. Remind them what you are looking for. Remember, they are busy if they are successful, and they might not always remember you. You might have to remind them of what you do and how you can help them in their business. Personally, I don't like to call them during the day and interrupt them. It also can interrupt my day. I prefer to call their offices late at night and leave a voice message. That way they can listen to it first thing in the morning – it's like they get to start their day off with me reminding them of a creative way to do business. It might say something like this:

"Hi Kathleen, this is Wendy Patton. I wanted to say 'hi' and let you know I was looking for another home that I can purchase on a lease purchase. Do you have any sellers right now that might be able to consider this type of solution? If so, please give me a call. My number is xxx-xxx-xxxx. Thank you, Kathleen, and I hope to talk to you soon."

If I haven't done business with them yet but I have been trying to start the relationship with the first deal, I would say something else like,

"Hi Kathleen, this is Wendy Patton. I am still looking for a home and I was wondering if any of your sellers have said that they might consider renting their homes if their home doesn't sell soon. I know most of your sellers do want to sell their home outright, but if you do ever hear one of your sellers say they might rent it, Kathleen, do call me. I will make sure you get your commission in full," and continue with this if you aren't a licensed real estate agent,

"Also, Kathleen, you will get to 'double-dip' on the commission and receive the full buyer agent portion too when it closes on the back end. I don't have a Realtor® involved. I will write up the offer, but you can have the entire commission. If your sellers rent out their home, they might not sell it and neither one of you would really get what you want. I would love to do a lease with an option and make sure you both get paid in full. Please keep me in mind if this type of situation comes up. This usually works well for any type of seller that does not need their cash out at closing to move on to their next home. Thanks so much Kathleen. Feel free to call me with any questions. My number is xxx-xxx-xxxx. Again that is xxx-xxx-xxxx."

Following up is key with Realtors®, however, don't be a pest. I would recommend no more than one time per month to remind them of what you do or to call them, maybe even every other month, especially once you have the relationship established. Each time you call them you don't want to say the same thing. You might try another version or way to explain how options or creative deals work. Another example might be,

"Hi Kathleen, this is Wendy Patton, just checking in to see if you have any sellers that might not need their cash out of their home at closing or they might be financed near 100%? If so, my type of solution might work well for them. Give me a call on any homes like that so I can set up a time to go and see them. I hope to talk to you soon on one of your listings. Kathleen, thanks for the opportunity to work with you. My number is xxx-xxx-xxxx."

Wendy's Advice

Getting a real estate license might be key for you. Check out my article on this subject by clicking here.

Ethics with Realtors®

Honesty and integrity with Realtors® will be the key to successful relationships with Realtors®. If I'm out there jerking Realtors® around, it's going to ruin my reputation and ruin the business for everyone else, so ethics in real estate is really important. Real estate is a small world and word gets around if you stiff a seller or walk away from a contract and tell them, "Go ahead and sue me." Realtors® find out, and as previously mentioned, they control 80-90% of the homes on the market. Do you think they're going to want to work with you? And even if your ethics are good, if Realtors® hear horror stories about deals gone bad because of investors who reneged on their lease options or lease purchases, it just ruins the market for the rest of us.

If you've committed to something with a Realtor®, get back with them and do it. There's nothing worse than going to a group of Realtors® with a presentation, they give you ten leads, and then you never get back with them regarding what happened with those leads. The Realtors® will wonder what is the point of helping you with leads if you don't follow up. It's the surest way to kill the rapport you have worked to establish. Did you look at the properties? What did you think? Are you interested? Are you going to pursue? Follow up and let the Realtors® know! Even if you don't have time to look at the properties, or they weren't what you were wanting, you should just communicate that and keep the lines of communication open so that they will continue to provide you with more leads. That's what you want from them – *leads!* They won't give you leads if you are not considerate to follow up with them about the status. The relationship needs to be a two-way street. They give, you give. And the more *you* give, the more they are willing to give.

There have been times when I have had a Realtor® call me about a "dumpy" property. I went look at it and knew it was over-priced. Now I'm faced with a dilemma: I don't want to insult the Realtor, because I want to keep that relationship positive; however, they were the ones who called me about the property. The best strategy is to be honest with them. I would say something like this,

"Sally, I looked at the home on 123 Main Street today. Boy, with what it needs, and what I think I can sell it for, and my carrying costs, the most I could offer would probably be an insult to the seller. I certainly don't want to affect your relationship with the seller. I think I will have to pass on this one, unless you *want me to still write it up. I will leave this up* to you*."*

See how I leave it up to them? I explained my reasons in terms that the Realtor® would totally understand without being insulting to her or the property. Not only that, but I've left the lines of communication open in such a way that the Realtor® will call me back one way or another regarding the house. This is what I want: I want them to continue to call me because they are my first relationship. Forget the house! Many times, they know it is overpriced anyway and just want an offer to show the seller, but at the same time I don't want to insult them. If they want me to write up an offer I will. If you are not licensed, the Realtor® will have to write it up for you and be your agent, too. Many times what happens with these types of deals is that the seller will eventually reduce the price and the agent can finally sell the home. I then have helped the Realtor® make the sale. Sometimes the seller doesn't think their home is overpriced until they get an offer from me and are shocked into reality. This might not help you as an investor today, but it probably will help you with the Realtor® for their next listing. Keep in touch with them and realize that being an investor is a long-term strategy and building relationships is also long term. For me, that one home is just a home. I want the relationship, so that they will bring me five more homes down the road. Rapport building with Realtors® is an essential part of the long-term big picture of investing. Stick to the program, work it one day at a time, and build your relationships for the long run. Investing is about Future Financial Freedom (FX3).

CHAPTER 9

Closing Deals with Realtors®

Why Aren't Lease Options Appealing to Realtors®?

When I first started doing lease options with Realtors® back in the early 1990s, it was a strong market in Detroit, but I wasn't getting very many leads from Realtors®. This both puzzled and bothered me because I thought I had something great to offer them.

I went to my best friend, Debbie, who is a local Realtor® and said, "Deb, look what I'm offering these Realtors®. It's a great thing for their sellers! Why aren't they all coming to me with their deals?"

She looked at me and said, "Wendy, do you truly believe it's a great deal for the Realtors® if they have to wait three to five years for their commission? They may not even be with the same real estate company when the house closes. This is a HOT market, they will probably sell their listings to someone else and get paid before then. They're not motivated to work with you on these types of deals. Why should they wait for years for their commission when if they just wait for a couple more months possibly weeks on the MLS they'll get their full commission now?"

I replied, "So what should I do?"

She said, "You're creative. Think of something."

I said, "You mean like pay their commission up front?"

She responded, "That would be a really good start."

And that's when I started paying their commissions up front and my ability to purchase completely turned around, especially in a seller's market.

Addressing the Commission Issue

Realtors® are not greedy, but they do want to be paid for the services they are providing for their sellers.

1. They are thinking about their sellers, and

2. By contract they're not entitled to their commission until the home closes. If closing is a number of years down the road, what's the likelihood that the Realtor® wants to wait that long and what's the likelihood that they'll even be with the real estate company that they are currently with (the deal is with the real estate company, not with the Realtor®). In most states, if a Realtor® leaves one agency and goes to another, they may forfeit their commissions. This makes this strategy unappealing for Realtors®, primarily in a HOT market.

The Realtor's job is to look out for their seller's best interests, and many Realtors® don't feel a lease option is a good solution for the sellers. If the Realtor® is simply dead set against it, just move on. However, there are lots of Realtors® out there, and there are many who are creative enough to want to work on finding innovative solutions for their clients. You just have to help them understand when to do that. If a seller is adamant and won't do it, also move on. Only spend your time on the ones open to the idea.

The reason why most Realtors® don't know about creative solutions and can't help their sellers consider a lease option or a lease purchase is because most sellers ***can't*** consider a lease option or purchase. Most sellers do need their cash out in order to buy the next home. I would estimate that only five to ten percent of sellers can consider a lease option because these sellers ***don't*** need their equity out of their home to buy their next home. The sellers that can consider a lease option or lease purchase usually will do it for two to five years in a seller's market and three to ten years in a buyer's market. This is a "Wendy Patton estimation" based on my experience and my students experience around the country. The seller's situation will determine the length of the lease option, the payments, price and other terms.

For those sellers where a lease option is a viable solution, the next hurdle is to insure that their Realtor® will benefit from the deal as well. We must keep the Realtor® in a win/win situation, and keep that positive rapport with the Realtor® for future deals.

In a seller's market the letter would look like this:

Dear Sally, *Date*

Would you like to sell your listing at (address of property)?

Maybe we can help. We buy homes especially when your client can accept terms like a lease /purchase. As soon as your client says to you, "If my house doesn't sell soon, I might have to rent or lease it," this is a great indication that our services might help you sell the listing.

When your client sells their home to (Your Company Name)…

YOUR COMMISSION IS PAID UP FRONT

and it would be a guaranteed closing for your seller. When would a client be able to accept a lease purchase? Here are some situations:

1. *They don't need their cash out yet but would like to either have cash flow or their payment made or*
2. *They have very little equity (i.e. financed near 100%).*

We have many references from clients like yours and from other real estate agents, including Agent 1, Agent 2, Agent 3, etc. Please talk to them to find out *how easy it is to sell a home to Your Company Name. Give us a call if this type of solution might work for your client.*

Sincerely,
Your Name

In a buyer's market I would use the words *lease option* and I would also say their commission is *paid in full* versus *up front*.

After I started to send out this type of letter the deals started to come in – especially when the commission was no longer a stumbling block issue for the Realtors®. They didn't have to worry about waiting for years to be paid for the work they were doing then.

Now, in a weaker market or a buyer's market, I don't pay their entire commission upfront. I might only pay part of their commission up front. I might pay one to one and a half percent versus three percent in a seller's market. They then would have to wait for a portion of their commission until closing. In a weaker market they realize that they might not get paid at all if their listings don't sell. The other reason for the lower payment to the Realtor® is that I am getting less from my buyers in these markets. Remember, slower market for sellers = slower market for buyers less money for sellers = less money for buyers. Realtors® understand that when business is slow for them, it is slow for me.

Example: I offer $200,000 in a seller's market and am paying three percent of the listing portion of the commission up front. This is $6,000. I would owe $194,000 when I pay off the seller when I exercise my option. If I don't exercise my option, however, I would not get that money back.

Structuring the Deal for the Realtor

Understanding the current economy is essential for making the offer work effectively. For instance, know whether you are in a strong buyer's market or seller's market so that you can structure your offer appropriately.

Seller's Market

This is the market where things are selling quickly, appreciating strongly, and sometimes multiple offers on the same house on the same day. This is also a time when the economy is good, things are happening, new construction, etc. When homes are selling quickly, Realtors® are getting paid quickly and in full – so in the beginning of a lease purchase, I offer to front their commission *in full* - Realtors® prefer a Lease Purchase in a strong seller's market. Lease Purchase means you are guaranteeing you will buy that home, so don't do it unless it's a strong seller's market, good appreciation, or you're positive you want to buy that home.

Buyer's Market

A strong buyer's market is the opposite: things are not selling, things are slow, unemployment is higher, homes are sitting and sometimes going from one Realtor® to another in an attempt to sell, and there's little or no appreciation, even depreciation…the Realtors® are not getting their commissions. Now the Realtors® are much more willing to negotiate because they're likely to lose their listing, and the sellers know that things are slow which is making them more anxious. This is a great lease option time.

During this time I only offer part of their commission up front, possibly part in twelve to eighteen months, and the rest at closing. When I say "I front it," however, the fee is really coming out of the option fees that the tenant-buyer pays to me and not out of my own pocket. When I assist the Realtor® in getting paid, they are more likely to work with me. The rule of thumb is: weak market = weak offer, strong market = strong offer. Always be fair.

Sequence of Events When Working with a Realtor®

- 1st — The Realtor gets a listing with a seller
- 2nd — The seller says the 4-letter word 'RENT' and the Realtor shares it with me
- 3rd — You look at the property
- 4th — You then negotiate the lease options deal through a proposal
- 5th — Agree on the terms
- 6th — Write up a full offer
- 7th — The offer gets signed
- 8th — You find a tenant buyer
- 9th — You pay the commission, or portion of commission, to the Realtor
- 10th — Tenant Buyer moves in
- 11th — Closing happens down the road

The Realtor® gets paid when I put someone in the home, therefore, when I get money from someone else.

The sequence of events is as follows:

Sometimes I say, "I'll commit but not until…" and I give them a future date because I need time to find a tenant. Even if my tenant doesn't move in by the start date, I am still responsible for paying the full commission on that date. It is stronger to a Realtor® and to the seller if you commit to starting on a certain date, regardless of whether or not you have a tenant. If there is no tenant-buyer, the commission will come out of your pocket – not exactly zero down for you the investor, but it is still a "low down" deal. If you have a tenant-buyer, the commission you need to pay will come out of the option fees of your tenant-buyer. You'll have to decide what risk you can take and afford when the start date comes.

If a Realtor® is working with a non-Realtor® on a sale, the Realtor® will be glad to wait for half of the commission up front but they won't wait for all of it on the back end. They'll wait for a double dip, however. A *Double Dip* is when the Realtor® gets the portion from the seller AND the buyer. If you are not licensed, the Realtor® would get both sides of the deal. Additionally, I need to be very clear about the payment to Realtors®. It isn't the Realtor® we (the investor) pay but the brokerage the Realtor® works for. The Realtor® gets their commission cut through the brokerage.

Structuring the Deals – The Details

Proposal – This is used to put together a mock-up offer to a Realtor® that they can then present to the homeowner or seller. It will put down the overall terms in writing without the specifics. This saves a lot of paperwork because you only fill out the other paperwork *when* you have an agreement on the proposal.

Here is an example of one of my proposals to a Realtor® or a Seller:

Your company name, LLC

Proposal

123 XYZ Street

Innovative approaches to Leasing/Selling

Your Company's Name has 2 programs to offer you…

Please review the following options that we can offer you as a Seller and consider which would serve you best!

Lease with an Option to Buy to Your Company Name #1
Your company name can pay you a monthly fee of $ 850.00 for a lease term of 3 years. We would then have the right to purchase your home within the 3 year term at a price of $126,000.00. $XX will be applied each month towards purchase price.

Lease with an Option to Buy to Your Company Name #2
Your company name can pay you a monthly fee of $ 900.00, for a lease term of 5 years. We would then have the right to purchase your home within the 5 year term at a price of $130,000.00. $XX will be applied each month towards purchase price.

In both of these options we would pay the rental amount whether or not the home is vacant or rented. You would still need to carry your homeowner's insurance and pay your property taxes until the home is closed. We would be responsible for everything from the date this agreement starts, including all maintenance (minor and major, except the first 60 days) of course change this if you want something different – for example they pay anything above $500. We would like to have all the appliances left with the home. At closing, you will need to pay the seller's title insurance, transfer fees/taxes (if any) and any other fees paid by a seller at closing. We also cover all utilities from our contract start date. We will start our rental payments to you when we find someone to place into your home; however, during this time frame you may also market your home for sale. If you sell it before we place someone, then this agreement can be voided by you.

Thank you for considering Your Company Name!

Your Company's Name

Your Company's Address

Your Phone number/fax/email etc.

Don't be anxious on the proposals – make it low-pressure. When you're first starting out, you'll want more deals to go through because there's a great excitement in the newness of the game. You'll be sitting on your proposals wanting a quick response. You'll be thinking of ways to use the money you're going to get on the backend if it all goes through perfectly. Although I do try to come up with creative solutions if I think there's a profit to be made, I don't sit on my proposals. It's a bit like testing the doneness of spaghetti – you throw it against the wall, and if it sticks, it's done. If your deals stick, they're done. If they don't stick, hopefully you've got others in you hip pocket that you're working on anyhow. Don't get too wrapped up in a deal happening, because a lot of them don't happen. I probably get about 40% of the proposals I put out- which means that 60% come up empty.

With some of the Realtors® I know very well, I might even do a verbal. For example, I might say, "See if the seller will go for $1,200 per month, and if they do, then I'll put together a proposal." You're just fishing a little bit to see if it's even worth sticking around in that spot or moving to another. If the seller goes for it, you hammer out a proposal, and if not, there are plenty of other deals out there!

Wendy's Advice

If it is meant to be, it will be.

CHAPTER 10

Finding & Qualifying a "Good" Tenant Buyer

Understanding how to screen tenant-buyers and select them is the key not only to being a good landlord, but also to the business of selling and using the lease option technique.

Finding and Working with Buyers – An Overview of Selling on Options

The weirdest thing about prospective tenant-buyers is that you can't always tell who is going to exercise by how well things are going with their tenancy. Some people do end up struggling to pay their rent and end up getting a mortgage on your home, and others pay perfectly and don't end up buying. You just never know.

I had perfect tenants in an eighteen month lease option and everything was going so smoothly I was sure that they were going to exercise the option. Then on month seventeen, I received a call from the woman and she was crying, she said, "We have got a problem. I can't pay my rent next month."

She was sobbing. She and her husband were getting a divorce and she couldn't pay the rent. She was very embarrassed and wanted a way to work things out in any way possible. Thinking she wouldn't be able to stay, I asked if it would be possible to start showing the house right away, and she said, "No problem. By the way, I do have some jewelry. Would you take that in exchange for my rent?"

My ears picked up. "Well, what kind?" I do like jewelry, but really I was thinking I might not ever get paid this rent, so perhaps I should consider this jewelry.

The wife said, "Diamonds and emeralds."

I said, "Really? When can I see them?"

She replied, "Well, how about now?"

When I got to her home I found out it was her anniversary ring and wedding ring. I said, "I can't take those!"

She said, "Really, I want you to have them. I can't pay the rent."

And I replied, "But what if you reconcile?"

She said, "We won't" and I said, "You just don't know. I really hope you will."

Now that just tugs at your heart a bit so I said, "Tell you what, I'll keep these for you. I'm a free pawn shop. I'll keep them a couple of years even, for FREE. If you ever want them back, just pay that rent, no late fees, nothing. Just take them. I don't want your rings."

The wife responded, “Oh no, I’m not coming back for those.” I said, “Well you never know. You might work it out. I want you to work it out.”

She said, “No, no, you don’t understand. I’ve been divorced twice now. From *him*.”

She never came back for the rings and I still have them. Maybe one day I’ll have them reset for my daughter. You just never know what you’re going to end up with in this business.

Finding the Best Leads for Tenant Buyers

Finding good tenant-buyers is the key to making the deal successful. There are many ways to find a good buyer for your home. Here are some of the ways that I use to market my houses:

1) **Advertise in the newspaper:** Try a few different ads. If no response, make changes and try again. Know whether you’re in a buyer’s or seller’s market. I have a friend who said in her ad “Free Pizza.” So people would call her up and say, “What’s this about free pizza?” and she replies, “Every month you pay your rent on time you get a free pizza.” It’s amazing what people will do for a free pizza.

How to Post a Successful Ad

Run an ad in the paper – “romance sells”- beautiful sunsets, bring your canoe – think of something short and catchy in the ad, things that might reflect a holiday or time of the year, or push on the credit issues, location, etc. There are so many ways to reach buyers. Try different approaches to see what works for you. If one ad doesn’t work, try another. If that one paper doesn’t work, try another paper.

This is a very generic ad – basic. It should appeal to a broad range of potential buyers.

Advertisement #1

```
Rent with option to buy this 3 bdrm, 1 bath home in xyz town near
xxx park. Large yard and view of lake. $1595/month and $5000 option
fee gets you in.
Bad credit ok.  (111) 222-3333.
```

Advertisement #2

```
Bad credit, no credit, poor credit, we can help. We have homes in
this area to help you get your credit re-established. Own a home
soon! Small amount needed to get in.   (222)333-3333
```

Advertisement #2 will bring in the buyer with bad credit. We are trying to find someone with poor credit. Not a deadbeat, just someone that needs another chance.

Advertisement #3 is the romantic type of ad. It is meant to draw in the romantics, young couples, etc. Each buyer responds to different ads, just like the sellers.

Advertisement #3

Sunset views with a bottle of wine help you celebrate your new home. Low monthly payments required $1395. Small option fee gets you a new start.
Call today (333)444-5555

Run advertisement #4 at the end of the year or the beginning of a new year. It is perfect to work on people's New Year resolutions.

Advertisement #4

Buy your family a new home in 20XX! Start out fresh! Own a home now! 3bdrm, 2ba in xyx town with great schools. $995 month and low amount required to get in. Call today. No bank qualifying
(333)444-6666

This ad contains my company website which is always good to put in an ad if you have one. Websites are one of the cheapest ways to advertise. It is great to direct buyers to a website where you can put pictures of the home or list other homes. You can do virtual tours on your website, additional homes, multiple properties, many pictures, and other advertising, etc. I also will give them information on how lease options work on this website. I am a Realtor®, so I have to disclose this in my ads, and this will immediately disclose that I am a Realtor® when they see my ads.

Advertisement #5

Stop Renting! Buy Now. We have several homes available with lease option terms. Oakland and Macomb Counties. Start building your future today. Homes ranging from $995-1995. We can help YOU!
(222)333-4444 www.MajesticRentals.com

Advertisement #6

```
Land Contract Wanted?   We have a home available on terms. Call for
a unique way to buy a home.  3bdrm home in xyx town.  $1,295 month.
$3,000 gets you in.    (222)333-4444
```

This is a great ad for parts of the country where the words *land contract* are used for seller financing. If your part of the country does use the term *land contract* then substitute the words *Seller Financing – no bank qualifying*. It attracts people that don't feel they can get a mortgage. They know they will need the seller to assist them in their financing. We are not going to give them seller financing or a land contract, but we are pulling them in from those words. We will discuss with them later that we are doing a lease with an option to buy and then they can clean up their credit to get a mortgage during this time period.

2) **Referrals from Realtors®:** You can get Realtors® to refer buyers to you.

Realtors® usually only work with buyers that can get a mortgage today and can go purchase a home from them. If they don't have a "pre-approval" letter, then they basically throw the buyers name in the garbage. I created a letter called, *A Piece of Garbage or $500.* The intention is to get Realtors® to give you the name and numbers of the people that come through their doors that they can't help; the people that can't buy a home traditionally through their office. If they refer them to me and they buy a home using a lease with an option from me, then I will give them that amount when they move into one of my homes.

You can further entice them by offering them more on the back end if they actually buy the home down the road. You decide how you want to run your business and what you want to offer, but Realtors® have leads on lots of these types of buyers. If you can't find them yourself, or if you need more, then consider bellying up to bar and offering to pay more. Remember, these are the Realtors® I want to find my sellers from also. Tie this all together now from Chapter 8 and 9, and see how powerful it can be to be working with Realtors®! They can bring you sellers AND they can bring you buyers – think of the possibilities!

3) **Websites** are one of the best ways to show your prospects the details of how options work, but also the details of a particular home.

Websites can also be used to show all of your properties when you get others. It is the least expensive way to advertise your homes. I am not a technical person, nor do I want to be one. You can buy a website for a low yearly fee and hire a high school or college kid to get a website set up for you. They are not expensive; yet, they can provide the viewers with a lot of information on your homes and services that you can't afford to print in a newspaper. Most people have access to the internet and have an email account.

4) **Signs:** Placing signs in front of homes that say *Lease to Own*, *Rent Option*, or *Lease or Buy*, etc. Also, if you have a home that is on a busy street or on a corner lot, put in the lease with that tenant that you can always put a sign out front to draw in tenants for other homes you have. Signs in front of homes do bring in calls for that home or others.

5) **Referrals**: Offer your current tenant-buyers free rent or option credit if they refer a friend that lease options from you. I prefer the option credit, because it is not cash out of my pocket and it entices them to purchase the home. If they don't purchase it costs me nothing; if they do it comes out of my pocket later.

There are many other ways to find tenant buyers, but experiment with them and see what works best for you.

Types of Tenant Buyers and Their Credit Situations

There are many types of credit situations that people have. There are four types of credit to be discussed:

1) Good
2) Deadbeats
3) Bad with Reason
4) Unknown

When a person has perfect or **good credit**, they don't need to consider a lease option. This technique is not necessary in order to buy a home. People with good credit can work with a Realtor® and buy any home they can afford. They also could find a home for sale by owner and work directly with a mortgage broker to get a loan. They have many choices. They don't need you!

The opposite of good is bad. **Deadbeats** are those that have poor credit and no excuse for it. They have the money but they just choose to ignore paying their bills at all or on time. They tend to be poor money managers or they are lazy and don't want to work to pay minimal bills. These are not the type of buyers we want in our home. They have habits and lifestyle changes that need to be made and you will not be the one to make them happen. Deadbeats are deadbeats! You don't need them!

Then there are those people that have **poor credit for a reason**. They are good people that had something bad happen to them. Bad things happen to good people. Bad credit can be caused from many different situations including: loss of job, divorce, medical problems with no medical insurance, disabilities, etc. These bad things can cause problems to an individual's credit. They have hit the bottom financially and are on their way up again. They have improved their situation, but not enough to go and buy a home yet. These are the types of buyers you will want buying your lease option homes. Bankruptcies are at an all time high in our country.

When a person files bankruptcy they may not be able to get a mortgage for several years after the discharge. People with collections or late pays on their credit report need time to heal these situations. Of course now there are more people then ever that went through a foreclosure or short sale. Many people won't wait until they can get a mortgage. In our country we tend to want things now. We overspend. Therefore, this might be why we are at an all time high for bankruptcy. This situation makes the selling of lease options an opportunity for us real estate investors. People want to buy now, but can't. They are willing to pay more for a home on an option, and have it now than to wait and save money. It is the "we want it now" mentality.

There are two things many people ask themselves when buying a car; how much down and how much a month. If those two things fit in the budget, then they buy the car. The price of the car being $28,000 vs. $26,000 was irrelevant. Homes are the same way. Therefore, the end price is not as important as the *terms*. Lease Options give terms to people with less than perfect credit.

The people that fall into the **unknown category** need to be evaluated more carefully. They have poor/bad credit but it is unknown as to whether or not they have improved their situation. The credit is still bad, but there is a reason. I would recommend you stay away from those people or have a lender evaluate them first. If a lender can't tell you if they are improving and will have a chance to get a mortgage, then I would recommend you stay away from them now. I would further recommend they hold tight for a few months and re-evaluate their situation to see if it has improved or changed. We want the people that had something bad happen to them, but they are on their way to repair and improvement. They are on their way up again.

Qualifying the Good Buyer

You are not looking for a bum when you run their credit; you are looking for someone that had a blip in their credit and now they are on their way to financial stability. When you look at someone's credit, see if they are on their way up or not. You can see what they have paid recently and what is still behind. This will show up on their credit report. Learn to read credit reports and get set up on a system that works for you. If you don't know which system to use, talk to others in your real estate investors group. They will know which companies provide which services in your area. You can also work with a mortgage broker to run credit and do the lease option approvals.

Your Standards

HUD (Housing and Urban Development) requires that landlords and employers have their standards in writing. If you don't have your standards in writing (and unfortunately few landlords do) then you are liable to end up in a pickle if someone accuses you of violating this rule. Your standards do not have to be complex but should be able to be produced if someone at a local or federal agency or anyone off the street requested a copy of them.

They might be something as simple as this:

Qualifications for Tenant Selection for Majestic Realty, LLC – Lease Options

1) *No Landlord Tenant Judgments Unpaid*
2) *Ability to Pay All Outstanding Judgments/Collections*
3) *Good Landlord Reference*
4) *Gross monthly income equal to 3 times monthly rental rate*

5) *If any Bankruptcy – Must be Discharged*
6) *Option Fee Available or Must be Negotiated/Financed*

Prefer they have spoken with a mortgage representative

On my lease option standards I don't put a credit score, but I do state that if they have a bankruptcy it must be discharged. I also don't put length of employment, but you can. These are my standards for lease options. My standards for my regular rentals are stricter. You have to establish your standards and they need to be in writing.

Screening a Good Buyer

Screening a buyer is extremely important and yet some of us investors still go by instinct or illegal decisions.

"We liked them," some investors will say to me. We want to buy from sellers that "like" us, but we don't sell that way. There are too many really good liars in the world and those of you that feel you can "read" people or rely on your gut feelings are set up for a rude awakening. Many of my worst situations came from my own desire to believe in people. We should all screen people as if we were blind and deaf. We would then screen them strictly on the facts and not our opinions or prejudices. Things to look for:

- Screen a tenant by **reviewing their application** thoroughly. Check it for accuracy and make sure they did not lie to you. If someone lies to me, they are denied the occupancy.

- **Check their name** – get a copy of their driver's license.

- **Check their landlord history**. The current landlord may want to get rid of them, but the previous landlord has nothing to hide. Call them both! Confirm it is the real landlord by one of two ways: check it on county records, or call the person and say a different amount of rent than on the rental application – example, "Hi, my name is Wendy. I am calling for a reference on your tenant named Joe Smith. Can you tell me how long he has rented from you? How does he keep your home? Has he been a good tenant? Would you rent to him again? Also, I see he pays you $900 per month, right?" Actually the application says $700 or something else. If this is Joe's friend, he will say, "Yes, that is right, $900 per month", if it is the real landlord he will correct it, "No, Joe only pays $700, did he say he paid $900?" Then I said, "Oh, no I see you are right. It does say $700, I miss read it. Thanks so much for your information."

- **Check their employment** – I use the same technique when I verify their income as I do their rental amount. When I contact the employer I say, "Joe put on his application that he is making $16.00 per hour, is this correct?" when he actually put $12.00 per hour. Trust me, if it is his employer and not his buddy they will correct you on this one! On occasion I will also ask for the most recent pay stubs to put in the file. This information is also handy to have in case you ever have to garnish wages. Make sure to verify hours they work and time on the job as well.

- **Check their banking information**, you might need it later.

Know What Are Reasonable and Unreasonable Expectations

Many of my tenants have pets and most of them smoke. For this reason I never say "no smoking" and "no pets" because I wouldn't have many of my tenants. Smoking and pets don't make people bad prospective tenants. However, here are some things on their application to look for that are potential smoking guns for bad tenants:

1. Why did they move? When a prospective tenant says they had a "bad landlord" before, it puts up a red flag to me. I know there are bad landlords out there, but the red flag it raises is that they are blaming someone for their problems. So I look further to see if there are other instances of blaming. If their business went into foreclosure are they blaming their accountant? If they have tax liens are they blaming the IRS? Be especially watchful for the blame game.

2. How long have they both had their current jobs, and how long did they have their previous jobs? What is the salary they are currently making? If they haven't been employed very long in their current situation, call their current employer to get an employment verification. Get the verification from an executive in the company or from the CPA/Accountant. Do not get it from the receptionist! Get the start date of employment as well as the current salary.

The Credit Report

Run a credit report and see what's going on with their debts. Some people may have medical issues that have caused them to have their current financial difficulties but credit scoring overlooks these. What is more important are repossessions, foreclosures, bad credit card debt, judgments from landlords etc. If they have a string of bad debts, you could be the next bead on that string.

The credit reports I receive have bad debts shaded and good debts in white. I would like to see a lot of white on the page. Too much shading indicates a lot of current and potential future problems.

1. Do they have frauds on their report?

2. Do they have bankruptcies on their report? This is not necessarily a deal-breaker, as bankruptcies can happen to even the best people and can sometimes be out of their control. However, the important question is, what are they doing to repair the bankruptcy?

wendypatton

Criminal Background Check

I don't run criminal background checks, even when the tenant "looks" like what I would consider to be a criminal. If you do one you must do them for all.

One of the first houses I ever bought was up for showing. Two rough-looking guys on Harley Davidson motorcycles drove up right onto the lawn and wanted me to show it to them. I was just twenty-one years old and feeling a little intimidated by these big, scary guys. They ended up renting the house, however, and they paid their rent perfectly on time every month as well as leaving the house better than when they rented it. Looks simply don't count. You must turn a blind eye and only focus on the qualifications on paper. In that spirit, you should also be thoroughly versed in the current fair housing laws.

What You Should Know About Fair Housing Laws

Fair Housing laws are an entire seminar in themselves. Realtors® around the country have half- to full-day training sessions on this topic alone, because fair housing rights, when violated, can cost owners hundreds of thousands of dollars. This is not an area where you want to mess up. The bottom line is this: select a tenant on their application alone and nothing else. There are federally protected areas and there may be some state protected categories also. Each state has their own protected areas, so check your state for the details. Your local real estate investors group can help point you in the right direction.

The way to be really safe is don't judge anyone by the way they look or talk. This is why I say that we should be blind and deaf when selecting a tenant. If we would just evaluate on the application process alone, then we would stay out of trouble. Then the selection would be based truly on the facts not our gut feelings or our instincts. Besides, many times our intuition is that someone is "good" and they later are "not so good". Stick with the law and you will be safe.

The federally protected categories include:

1) Religion
2) Race
3) Nationality
4) National Origin
5) Color
6) Sexual Preference
7) Marital Status
8) Age
9) Weight/Height
10) Familial status – while you can't ask a potential tenant how many children they have, you can ask how many people total will be residing in the home. You don't have to rent your two bedroom home to a family of nine.
11) Handicap

Be extremely careful with this area of federal law. Even an inadvertent misstep may haunt your career for a long time.

Rejecting a Rental Applicant

If you reject someone's application, you have to tell them why you rejected them in writing, and there is no need to obscure your reasons. Be honest and be kind. Let them know that if they can clean up some of their credit difficulties, that you may be able to help them in the future. If you feel inclined, you might even suggest they talk to a lender or financial counselor about how they can get their credit report into a more favorable position.

Buyer's Objections

Although tenant buyers will rarely have any objections to want to rent from you, there are few that should be discussed. You will need to know some ways to handle these objections and what you can say to your tenant-buyers. Here are a few of the most common:

What happens to my option money if I don't buy this home? It's non refundable. This house is going off the market during the option period, so there's a fee for that. We are providing a service and for this service there is a fee. If you are not sure you want to buy this home, you should not put an option fee down on this home. You should rent from someone else. We want to sell this home to someone that wants to buy it in the future. You do want to buy one day, don't you?

What if I can't get a mortgage? Then you would lose your right to buy this home. We do have the right to extend or give you another chance to buy this home, but at this point we are not guaranteeing anything. If the market does go up, we also might increase the price of the home. We are only fixing the price and terms during the time period we have signed here today.
But, you can talk to another lender if they are working with someone other than you recommended. Sometimes you can get them approved with someone else. It is usually a requirement of all lenders to pay off judgments, liens and collections before qualifying for a mortgage.

I don't want the potential tenant to putz about making a decision, so I always say that I have other people looking and that my advertisement is running, so they need to decide what they're going to do and how interested they really are. After all, they are the ones in trouble, not me.

There are times when you will find the buyer does not have the full amount to put down on the option fee. Be creative on the option fees. I've taken two mobile homes in trade for option fees. I'm not in the mobile home business and I hate them, but it got the deal through! You can also work on monthly payments with them. You can take an extra $200 per month towards the option fee until it is paid in full, however, you should always get more upfront then what you would have received if you were getting a security deposit. Don't ever do less than that.

Once you have your terms determined and your *Good Tenant* selected then you must get the paper work ready and signed. Get them locked in and set for the move in date!

CHAPTER 11

Getting the Paperwork Ready for the Tenant Buyer

Approved!

Once you have approved a tenant for your lease option home; all you have to do is draft the paperwork and have them sign it all. You need not give more than twelve to eighteen months to the buyer on an option. This time frame is most often enough for a good option tenant to get a mortgage. For you, the benefit in keeping it short-term is appreciating markets. Whatever appreciation is written into the contract is what you have to stay with regardless of whether or not the market is higher. Appraisers also have a five to ten percent leeway on appraisals. While I could structure a long-term option deal that said the value or the mortgage would be dependent on the year appraisal growth rate, by whose appraisal would it be valid? If it's my appraiser, the buyer may feel taken advantage of, and if it's the buyer's appraiser, the appraisal might be too low. So keep it short and sweet. It avoids problems.

If at the end of the time period your buyer wants to extend, it is at your discretion to decide if that is what you want to do. This can also be an opportunity to renegotiate. If the homes in that area have appreciated more than you expected, then you would want to extend, but increase the purchase price somewhat. Secondly, you could also ask for another $500 to $3,000 option fee for the convenience of extending the option. Finally, you could raise the rent slightly. There are times I have given my tenants an extension for free, because of circumstances. There are also times when I have said no.

It all depends on your circumstances and theirs. If you give the tenant longer than eighteen months then you are obligated to offer an extension on the option. You can always offer that later, of course, but there is no reason to obligate yourself until that time comes and it still works for you. You can't predict what the market will be like in the future, so getting further out than that can be more risky for you, and you forfeit your ability to sell the property outright at the end of the option.

If it is more than a few days between the end of the option and the day they plan to move into the home, your best bet is to get a non-refundable deposit from them to hold the home until the move in date. This protects you from them changing their minds at the last minute. A personal check at this time is okay if it has time to clear before the move in date. Take a copy of the check for their bank account information. If they end up ditching the home and owing you money, you will know where to garnish their bank account.

Have all the forms ready to go and printed. Get the tenant to sign early if possible. Depending on how busy you both are; try to get them all signed after they give you the deposit.

When you are working with the buyer, you are the landlord to them. You are also the seller, as far as they are concerned, because you have set the terms for the sale including the option fee, the monthly payment, and the sale price. Because they see you as the seller, you need to use pro-seller forms. These are forms that specifically favor your end of the deal as the seller.

Getting the process started!

At the beginning of this deal you have either optioned the home from the seller and have in turn optioned it to a tenant-buyer or you own the home outright. I mentioned before how important I think checklists are in processing lease options—no matter how many you have completed! Let's look at my Selling on a Lease Option checklist, then each step in more detail:

Selling On An Option Check List

ADDRESS:___________________________________
MOVE IN DATE:_____________________________
Seller Name:_______________________________________
Phone:____

1. Advertise Home
2. Get Application Fee
3. Get Application
4. Confirm Applicant Meets Criteria
   If not, send Rejection Letter
5. Get Non-Refundable Deposit and Non Refundable Deposit Form if Accepted
6. Create Tenant Folder
7. Draft Contracts
8. Video Tape Home or Take Pictures
9. Get Check in/out List
10. Sign Contracts
11. Sign the Lead Based Paint
12. Sign the Sellers Disclosure
13. Cancel Advertising
14. Confirm Utilities in their Name: H_2O ___ Gas ____ Elec ____ H_2O Softener ___ other ____
15. Confirm Check in/out Returned
16. Confirm they have Renter's Insurance
17. Remove Sign and Lockbox
18. Make a Copy of Tenant's Check for Tenant File

1. **Advertise the Home**

2. **Get Application Fee**

3. **Get Application:** Make sure they fill out all areas of the application completely. My application will request information on each applicant over the age of eighteen, even if they are not working.

   It will ask for their drivers license number, social security number, employment information, banking information, landlord or current address information, and previous landlord information. The more information you can gather, the better off you will be if you ever do need it. It is not so much needed for your evaluation, because that is done on standards you have set in Chapter 10, but if you ever to have a problem with a tenant and need to later collect from them you will want complete information on this application. Make sure it is completely filled out and signed by all parties.

4. **Confirm Applicant Meets Criteria:** See your standards from Chapter 10 – it is a yes or no.

5. **If not send Rejection Letter**: Rejection notice is required by law whenever anyone applies for credit or a place to live. You must specify why someone is not accepted whether it be landlord history, income status, credit issues, or anything else not federally protected by law. You must be specific.

6. **Get Non-Refundable Deposit and Non-Refundable Deposit Form if Accepted**: Once someone has decided they want to move into one of your homes but may not move in for a couple of weeks, be sure to get a non-refundable deposit. This is separate from an option; however, it later will be applied towards their option. The non-refundable deposit holds the property and shows their intent to rent it. If they don't later sign their contracts or move in they would lose this deposit.

7. **Create Tenant Folder:** This will be the right-tabbed red folder. I call this the tenant folder, whereas the green ones are for the owners. I use legal size and half tabs so I can put the address either on a white label with a red strip on the top of the address, or you could put the address in red or green themselves. All information on the tenant and their contracts and correspondence will go into this folder.

8. **Draft Contracts:** Draft the rental agreement, option agreement, sales agreement, pet agreement (if they have a pet, lead based paint, and seller's disclosure) and any other state required forms.

9. **Video Tape Home or Take Pictures:** Do this with the tenant if possible or get pictures. I suggest that you take a video camera with you when you are showing prospective buyers the home. Say things on the video like "Marie, what do you think about the kitchen cabinets? Marie, what do you think about the bathroom tile? Marie, what do you think about the closet doors?" – and you've got dates on the video to prove everything so that Marie can't come back later and say, "Those kitchen cabinets were trashed" when she says on the video that they are fine. Any pictures that you take should be kept on a CD in the tenant file for that house. After we take complete pictures of the home inside and out, we put the disc into a special holder inside their file. Those pictures are really to protect you later if they don't buy the home and if they've done damage to the home.

10. **Give Check In/Out List to Tenant Buyer:** The check in/out list is basically a form that the tenant can fill to evaluate the condition of the home when they move in. This is a base-line of the home and its condition. It is to protect you both in the event that they don't purchase the home and they decide to move out. It will show the condition

of the home at the time when they move in (also use #9 above for this). Each state will have different requirements for what judges will require and allow, but the more you can show on the condition, the better off you will be if you are trying to collect on damages the tenant has done. Go overboard versus under-board on documentation and pictures. You hope you will never need them, but if you do you will be glad you have them.

11. **Sign Contracts:** The buyer needs to come in and sign each of the contracts with you. If, however, they have already paid their non-refundable deposit, I will allow them to take the contracts and review them. They need to be signed before they move in.

12. **Sign the Lead Based Paint** – See Chapter 6 for more detail; however, you can create a new one that is blank and says you don't know anything about lead in the home, if this is true, and sign it. You can also attach the previous owner's lead based paint and have the tenant buyer initial it to acknowledge they have seen it. This is federal law.

13. **Sign the Seller's Disclosure:** If it is the first time that you rented the home you may not know much about the home and you can write on the seller's disclosure that you have never lived in the home and the buyer should do their own inspection, and the home is being sold "AS IS;" however, I would also recommend that you attach the previous seller's disclosure to it (a copy of it) and have them initial it. You will know what the seller disclosed to you. You need to disclose everything you know. Also, if you have had it a while and then the roof starts leaking, you must disclose that, even if you fixed it. I can't stress this area enough! There are many lawsuits going on in our country today because of lack of disclosure when the sellers *knew* about problems and didn't disclose them. If you had a leaking basement and fixed it, you need to put that on the seller's disclosure. It won't stop anyone from buying the home if it was fixed, but if it leaks later and they find out it wasn't disclosed, you will be fixing it again, versus if it was disclosed, they would be fixing it.

14. **Cancel Advertising:** Cancel any advertising you have on the home. Sounds simple, but it can be expensive. I have forgotten to do this, and it can cut into your profit if this is not on your checklists.

15. **Confirm Utilities Are On:** Once the tenant has moved in, make sure they have transferred the utilities into their name, including gas, water, electric, water softener.

16. **Confirm Check In/Out Returned:** Make sure you follow up and get this returned from your tenant-buyer. If there is anything on the check in/out list that needs to be addressed then take care of it.

17. **Confirm they have Renter's Insurance:** If not, continue to follow up in writing with them and put a copy in their tenant file. It probably won't be a make or break for you, but if something where to happen to their personal belongings, for instance, you will have all the proof you need that you tried and tried to protect them, but they failed to protect themselves.

18. **Remove Sign and Lockbox**

19. **Make a Copy of Tenant's Check for Tenant File:** You might need this later if you need to garnish their bank account to pay off a debt to you.

Always Check Your Paperwork!

My partner, Debbie, and I purchased a property on Newman Street. The little house had 900 square feet with a walk out basement to Paint Creek. The owner was an older woman whom had split the lot and a developer was going to put something on the empty property. The vacant lot was the same size as the one with the house. When we bought the property, I knew up front that the owner was going to sell the vacant part to a developer. We lease optioned the house to a couple who gave $5,000. As happens many times, everything was going perfectly and it seemed like they were going to exercise the option. Sixteen to seventeen months into the lease option, the couple called me and insisted, "You have to sell us the other property too."

When the couple had signed the lease-option, I physically walked the property with them and showed them what Debbie and I owned and what we didn't own, including the fact that we did not own the undeveloped part. They still said, "You have to sell it to us."

Standing firm, I reiterated that only the house and the property it sat on were included in the lease option, not the vacant split property.

At the end of their eighteen month option they not only didn't exercise the option but stayed on an additional three weeks without paying and then moved out. I sued for $900 for unpaid rent. They counter-sued for the refund of the lease-option money, again insisting that it was their right to buy the entire property. It cost me $1,500 in court but the judge awarded me their $900 in unpaid rent. The couple still refused to pay the rent and it ended up being scheduled with a mediator. Then the day before the mediation for $900, the couple called and paid it. End of story? OF COURSE NOT!

Two weeks later I got a call from the little old lady we bought it from who said, "We got a problem. You own this other property." It turns out that when I received the deed from Century 21 and the title company, both parts of the property had been deeded, although the vacant part was not supposed to have been deeded. We actually *did* own both parts of the property, just as the wife had insisted, and if they had actually exercised their option, they would have owned both parts. It turns out the wife worked for a mortgage company and had probably checked and thus, understandably, thought I was lying about not owning the other part of the property even though I honestly thought Debbie and I only owned half. What I had done was to take the deed I got from closing and copy the legal description for the whole thing and I put it right on my copy to her. After the case was settled, I deeded the vacant part back to the little old lady. The moral of this story is to always check your paperwork, especially legal documents!

What You Need to Know About the Three Essential Contracts

In each state you may have required information for your rental agreements and purchase agreements. My contracts are generic enough to use everywhere; however, they should still be reviewed by an attorney in your state. Each state will have its own landlord/tenant and security deposit laws. Therefore, as recommended, you should seek the advice of an attorney if you are using any generic contracts for your state to buy, sell or lease real estate. I recommend Pre-Paid Legal attorneys at www.Prepaidlegal.com/hub/Wendypatton They have plans starting at very reasonable rates per month to give you legal assistance, and I have been a customer since 1988 and have saved thousands of dollars to help me on legal questions, contract reviews, letters, etc. for real estate matters and in multiple states.

Each state has its own rules and regulations regarding rentals, lead based paint abatement, evictions, etc. There are so many more clauses when you are selling, especially the rental agreement, because there are so many more things you will need to do to protect yourself. When you are buying, the rental agreement is very short; when you are selling it is very long. Here are some of the clauses that have been my favorite over the years in my contracts to sell on lease options:

- *The Option Agreement* – On the buying side, the option agreement turns control of the property over to the optionee (the buyer) without ownership. When I am doing a lease option, I sign an option with the buyer. I control the property as if it were owned by me, but I am optioning them the right to buy upon exercising the terms of the option, usually in twelve to twenty-four months.

- *The Rental Agreement* - The rental agreement specifies how long the tenant will rent their home and how much they will pay each month in rent to me. It has to stay a rental even during an option period because the tenant doesn't control or own the property. A rental agreement also comes in handy if ever taken to court so that you can show the judge that no matter what the tenant has put into the property, the judge will let me evict if necessary rather than foreclose.

- *The Sales Agreement* – This agreement sets the terms of the final sale. There are two of these in a sandwich lease option – one for my deal with the seller, and one for my deal with the tenant-buyer. The deal with the tenant-buyer sets the sale price upon the buyer exercising their option. On the tenant side, the contract also has a solid number, and because you set the terms of the lease option, that price will be higher than the price you have with the seller.

Points to Consider for the Option Agreement

It is important to get the optionee (the tenant-buyer) to be as responsible for the maintenance and well-being of the house and property as possible so that you are not tied down with constant maintenance. Here are some points in my option agreement:

1. Optionee agrees to accept the property in "as is" condition.
2. Optionee agrees to make all repairs major and minor to the property.

3. If the optionor (the investor/seller) has to make any repairs to the property, the cost of the repairs will be added to the purchase price. If someone's water heater or furnace goes out and the tenant can't afford to fix it, you should go ahead and pay for the repairs. In Michigan, you just can't go without heat in the dead of winter.
4. If there is a septic system, the optionee agrees to have it pumped once per year.
5. If there is a pool, optionee agrees to open and close the pool each year and to maintain the pool.
6. Optionee should pay for all additional assessments including water, sewage, sidewalks and road paving.
7. The option can become void if the optionee pays more than ten days late. It is important to remind your tenants that their record of payments will have to be submitted to the mortgage company and may damage their ability to secure a mortgage. So, if they're serious about owning the home, they need to be serious about paying on time.
8. If the option is voided for any reason, then the agreement returns to a rental only agreement and is month to month so that I can take steps to resell the property.
9. Optionee agrees not to record anything against the title of the property. In other words, the tenant cannot file a memorandum on the property, and you definitely don't want them to do that.
   NOTE: If I am not the owner of the property, and if somehow the title work has gotten messed up so that the optionee is unable to exercise because they can't get the clear title, then I refund the option fee plus an additional $500.
10. You are not giving them equitable position – in other words, they can't go into foreclosure on you. You can, however, evict.
11. Advise the optionee to always seek the advice of a mortgage broker and an attorney before signing the document. The mortgage broker might look at their credit and their history and tell them that even for an eighteen month option they will not be able to clean up their history enough to qualify for a mortgage. They should also always have a lawyer look over any type of document that commits them to an agreement. In my experience, most people talk to neither, but they sign the document saying that they have.
12. Time is of the essence so the start of the option is only for a very brief period. You might have it be three days and say, "If I don't have the signed documents back in three days, I'll assume you're not interested."

Points to Consider for the Rental Agreement

The rental agreement gives the tenant the right to occupy the property during a time period. It will be similar to the rental agreement you signed with the owner/seller, except obviously your rental agreement with the tenant will be very pro-landlord (pro-you).

The rental agreement really needs to be separate, but only for selling on an option. If you are the buyer, you certainly can put them into one document, but when turning the option around, you'll want to use the three different documents. The reason for this is that if the tenant doesn't pay, or the deal goes south, you will want to be able to evict them as quickly as your state allows. If you have them all in one contract, some judges will look at the lease option as a sale rather than a lease, and therefore make you go through a full foreclosure or forfeiture process versus an eviction. This will be much longer, more expensive and may require an attorney. Therefore you will want to keep the agreements separate. Always prepare for the worst-case scenario, and then you will be ready if it happens.

Anyone who will be residing on the property over the legal age must sign the rental agreement. This includes children of legal age (as determined by the state).

Co-signer Agreement

This can be a good step to take if someone is a really weak applicant, but you know that they have a really strong parent applicant or friend who is willing to sign with them on their rental agreement. It works really well for giving liability to someone else, especially if someone is really weak. I have a situation where a mother co-signed for her daughter. It was just a rental but the daughter had terrible credit. The mother, however, worked for General Motors for twenty-five or thirty years and made a good guarantee person for me. The daughter stuck me for nearly $5,000 in unpaid rent and damages, and now the mother is paying for it out of her GM checks.

In another case, the mother was a local Realtor® in Michigan, and she came to me and asked me to help her daughter get a house. Her daughter had been through a rough time, and the Mom was willing to co-sign. I probably didn't even run the daughter's credit because I knew the Mother was a well-known Realtor® and was good for whatever might not happen. The mother paid the $5,000 option fee – and the rent was $1,300. Then the daughter left and ended up owing me $9,000 in unpaid rent and the mom is the one paying on it now.

A few more things to consider for the Rental Agreement

1) I like all of my rent due on the first day of the month. If I have a tenant that moves in on the 7th, then I will pro-rate the rent for the month. My rental agreements specify late fees of $25 for the first day late and $5 per day afterwards, and the tenant, of course, must sign the agreement to this. I can't reiterate how necessary it is to have everything in writing, spelled out to the minutia. That way your tenant can't come back to you and say, "I never agreed to that." All you have to do is point to the contract and say, "Here it is in black and white and there's your signature underneath it." I even like to add an incentive to encourage my tenants to pay on the 1st of the month. In my contracts it states that if they make their monthly payments on time, including any unpaid option fees, that I will credit them with $100 towards the purchase price of the house.

2) Your other fees on the property can include: pet deposit, security deposit, cleaning fees, etc. In a lease option, I usually do not require a security deposit, and the reason for this is that if they have an extra $1,500 for a security deposit, which is refundable, I'd rather have them apply that to the option fee, which is non-refundable. None of the option fees, however, show up on the rental agreement, as the option agreement is a separate issue. Your rental agreement must say how much the total cost is to move in. For example, if there are fees, you need to add the fees to the 1st month's rent, and that is your total on the rental agreement, but it is not the total overall since you need to add separately the option fee. The rental fees plus the option fees make up the total move-in costs.

3) The rental agreement must show the total amount of anticipated rent for the contracted period, including pro-rated months. Typically on my rental agreements, as I mentioned, I have a twelve to eighteen month period at the conclusion of which I hope they'll exercise the option.

4) Your rental agreement should say that the keys are due back within 24 hours if the tenant does not exercise the option. This is a way to protect yourself just as you would any other tenant.

5) You can also say that if the rent is late more than ten days that the agreement may revert to a month-to month rental (and nullifies the option) at the discretion of the landlord. I generally don't do this unless I want to get rid of the tenant, because when this alternative plan is set in motion that allows the tenant to move out at any time.

6) Payments should be postmarked by the post office rather than a Pitney Bowes machine as the machines can have their dates changed. In my rental contracts I also specify that any bounced checks are subject to an additional fee. Although I start off trusting my tenants and allowing them to pay with personal checks, one bounced check and after that all payments must be paid in certified funds or bank check only. I also tell them that if their rent is late two times within a twelve month period, their monthly rent will increase $25 per month.

   You should specify to the tenant how their payments will be applied:
   1. to outstanding dishonored check fees
   2. to outstanding late fees chargeable to tenant
   3. to outstanding legal fees, court costs or both
   4. to outstanding utility bills that are the tenant's responsibility
   5. to any damage caused by tenant
   6. to collection agency fees
   7. costs for re-letting the property, if applicable
   8. to option fees owed
   9. rent – the reason why you want their money to be applied towards rent last is because it is easier to evict on unpaid rent than on unpaid utilities. So use their money to pay for unpaid utilities, and if the rest doesn't cover the rent, you can begin eviction proceedings.

Additional Issues to Cover in Your Rental Contract

Occupancy: The contract needs to specify that the premises will be used as a residence with a specified number of adults and children. The premises will be used for no other purpose without written permission by the owner. Any guest staying more than fourteen days will be considered a breach of the agreement unless the resident tenant receives written consent from the landlord. I also don't allow them to use the premises for a home business without my permission. A lot of people have home-based businesses, and that's not a concern except if they have customers coming in and out of the home, which creates a potential liability issue. So, just check with your tenant to see what kind of home-based business they will have.

Pets: I make sure that they sign an agreement with me about having pets on the premises. I need to know, for example, if they have Pit Bulls or any other potentially dangerous animals on the property. It doesn't matter to me if they do have pets, and in fact almost all of my tenants have pets. I just need to know about it.

Entry and Inspection: This gives you the right to enter the property at reasonable times and with reasonable notice to inspect the premises. It's not that you are inspecting their personal lives but that you want to make sure the home and property, which do not yet legally belong to the tenant, are maintained in accordance to the rental agreement. You also may want to show the home to prospective new tenants or buyers. If the tenant decides not to exercise, you want to have right to affix "for sale" signs on the front lawn, and you can't even step onto the lawn without calling the tenant first as provided in the contract.

Assignment and Subletting: I do not let my tenants sublet or rent any portion of the premises without my prior consent. The subletter's name is not on the rental agreement.

Joint and Several Liability: Anyone who signs the contract is 100% responsible for all the points within the contract up to the total of whatever is due. I had three guys who signed the agreement and all three split later. I was only able to find one of them and I told him he was 100% responsible to fulfill the agreement. He felt he should only be responsible for his third, but this inclusion of joint and several liabilities protects the landlord from having to find all the tenants. If one can be found that one is 100% responsible.

Maintenance, Repairs and Alterations: It is the tenant's responsibility at all times to maintain the residence and property in a clean and sanitary manner including fixtures, equipment, appliances, furniture, and all other furnishings. If they should chose not to exercise the option, the residence should be left in the same condition as originally rented, except for normal wear and tear. Residents are responsible for changing the furnace filters and the batteries in the smoke detectors on a regular basis. Residents should be responsible for the maintenance of the property and the house costs. Then tenant cannot make major changes to the structure until he owns the property. I had one resident who tore off an upper decking because he decided he didn't want it, and I had to pay for it and then re-bill the tenant because I didn't own that house.

The resident also cannot paint, wallpaper or make any other changes without consent of the owner. I had one tenant who repainted the inside of the home navy blue, and then they left after two months. I had to sue to recoup my costs for repainting the home. Residents must also be responsible for the cleaning of sewers and drains that have become blocked due to their negligence to keep them cleaned.

You can have a co-pay system with your tenants regarding small fixtures, and you set the limit. Maybe you want to say that anything under $50 they need to pay for but anything over $50 you will cover all except the initial $50.

If the resident damages any windows or doors, it is their responsibility to replace those items immediately. If the resident hasn't repaired the items within seven days, I will replace the items and charge the resident for the repairs, and these costs will be due immediately. I tell my tenants that any repair under ten dollars must be reported to me and any repair over ten dollars must be approved in writing. In other words, they don't have an open checkbook to make any repairs they want. Make sure your tenant also doesn't run off and do repairs and then bill you for them, such as "My furnace went out and I paid the guy $200 to fix it." My furnace guy might only be $100. Also, the tenant may then try to take that repair bill and use it against their rent. Make it very clear to the tenant that NO repairs can be made without your consent if the repairs are over ten dollars.

Appliances: One of the things I list on the contract is all of the appliances already in the home. I make it clear to the tenant that all the appliances in the home are there for my convenience, not so much for them. In other words, those appliances belong to me. If, therefore, one of the appliances stops working and they dispose of it without ever telling me and then leave the home with that appliance missing, I will bill them for it. If they want to remove the appliance, I have to agree to it and I will cross it off their rental agreement with my initials and the date.

Ordinances and Statutes: The tenant must abide by local zoning laws for usage of the property. For example, they can't run a daycare out of the home if it isn't zoned that way (not to mention the excessive liability that would incur). A home-based business of being a web site designer, however, violates no zoning laws anywhere in the country. I have the right, as the landlord, to evict immediately for any illegal operations on the premises – for example drug usage or manufacturing. Even so, you must still follow legal procedure. The worst thing you can ever do is evict someone and throw their stuff out onto the street without going through the proper procedures because that can come back and bite you. No matter how annoyed you may be, you must always follow the legal course of action by going through the court system.

Liability of the Tenant: The resident is responsible for any personal injury or property damage caused by the resident, tenant or tenant's visitors. The tenant is also responsible for damage due to negligence of the property. If there is a fire, however, and all of the tenant's property is lost, the owner is not responsible to pay for that since the tenant carries his own renter's insurance for just such an event. The tenant must keep all the sidewalks clear and clean, all access to the home free and clear and should maintain the outside premises to be a safe environment.

Insurance coverage: Because the owner's policy does not cover the belongings of the tenant, the owner requires the tenant to carry their own insurance against the risk of damage to their personal property. This insurance must be in place before the tenant moves in.

Defaults – Landlord remedies: Let the tenant know that failure to comply with even one part of the agreement will constitute a default of the entire agreement. This means that the owner can immediately repossess the property.

Attorney Fees: In the event that either party has to make it a legal matter to enforce the terms of the contract, the owner will be allowed to recoup all attorney fees allowed by law.

Security Deposit Act (aka SDA): Make sure that the security deposit act from within your own state is in your rental contract. The SDA varies per state, and you must know what the rules are for your state. You are the one providing the contract, so you are responsible for that information. As such, it is also your responsibility to educate your tenant on what the SDA allows or doesn't allow. Going over the contract with your tenant is an excellent time to explain this detail.

Notices: Any notices must be in writing for your own protection and not verbal. Notices should be sent to the residence address and if the tenant is sending you a notice, it should be sent to the address specified in the contract (either office or post office box).

Waiver: Failure of the owner to not enforce any part of the contract will not constitute a waiver of the contract. For example, if I waive the late fee one month, that doesn't negate my right to enforce it the next month.

Holding Over: The tenant must give a 30-day written notice of intent to vacate the property.

Additional Terms and Conditions: Some further things to potentially add to your contract might include:

1. Vehicle limit
2. No motorcycles (some can violate the city noise ordinance)
3. No working on the car on the premises. All repair work to be done off site.
4. No permanent stickers on the bathtub and only non-abrasive cleaners to be used on the tub.
5. No carpet cleaners will be used without landlord permission. The reason for this is that some of the over the counter cleaning solutions can actually bleach the carpet and leave a white spot.

Make Sure Your Tenants Read and Understand the Agreement

It is very important when you are detailing your contract with the tenant that you go through it line by line with them so that they have heard everything out loud and are now responsible for the contents when they sign their name. Don't skip over any points of your contract, even if you see them begin to fidget because it does take a while. You might also ask after each point, "Do you have any questions about that?"

Purchase Agreement - Offer to Purchase

The offer to purchase is very pro-seller. Some things to consider in the purchase agreement include:

1. What items that are in the house will remain with the house (for example, appliances)?
2. You will want to protect yourself depending on the type of mortgage they get. If they get a FHA or other government mortgage, the mortgage might stipulate improvements to the property before it goes through. I don't want to be responsible for that, so I say clearly in my contract that they are responsible for any requirements needed to fulfill their own mortgage.

3. Make it clear that the tenant is buying the house "as is."

4. Tax pro-rations: Make sure it is pro-seller and is worded for your state's standards. In other words, you want to get any tax advantage so that the buyer pays all the taxes.

5. Special assessments come due now if you have paid them out of your own pocket. For example, if the city has required sidewalk repair and you paid for it, now you pass that back to the buyer.

6. They should have an inspection before they move in.

7. Make sure to give them the Seller's Disclosure Statement. This not only becomes a part of their history but will be then handed off to the next buyer as a complete history of the house.

8. Lead based paint disclosure!

9. If I default on their option agreement, they get their option fees back plus an additional $500.

Additional conditions:

- If you are a licensed Realtor® you have to disclose it.

- Purchaser should have a home inspection but if they waived their right, then I mark down the date they walked through the home.

- Anything that I have to do in regards to repairs gets added to the purchase price.

- Advise the purchaser to seek the advice of a broker and attorney before signing the purchase agreement.

- Pet Policies and Agreements -The pet policy and agreement is attached to the rental agreement and is signed on the same day. I have them list the names of all their pets. If one of their pets dies or is given away they don't have the right to just go out and get another one. The animal breeds should also be named. If they can give you a copy of the animals' health and shot/rabies records to have on file, that would be helpful were there to ever be a biting incident. If the local ordinance requires licensing, then you should get a copy of that also. Typically on my option agreements I waive any monthly pet fees, but in a pure rental situation, I might not be so lenient.

- Deposits for the property - If I get a deposit on a property, it is non-refundable if they choose not to option it. However, I do refund it they are rejected based on credit or the potential ability to get a mortgage. Most of the time I won't even accept a deposit until I know they're approved.

- Rental Application - Verify their Social Security Number and employer information

- Application fees: Have the tenant disclose any credit issues they may have when they apply for a home.

- The property inventory check in/check out list

Be Prepared For the Tenants

On the move-in date they deliver the final balance in certified funds. Don't take a personal check except on their deposit. Once they have moved in, personal checks are okay, but not on the initial option and move in date. The day they move in you will need to make sure the following is complete:

1) A copy of their renter's insurance
2) Keys for the home
3) Remove the sign and lockbox – if any
4) Make sure they have the utilities turned on in their name
5) Water/Sewer bills?
6) New phone number for tenants
7) Walk through the home and do check in/check out
8) Take pictures of home
9) Give move in gift (optional) could be a small plant, card, flowers, etc.

If the optionee wants to exercise the option, they must send a notice in writing to my offices. If however, they do not follow all the terms of the rental agreement, I can deem the option null and void.

This may sound like a lot of paperwork and considerations to keep track of, but it's all to protect you. Think of "pro-seller" as also meaning, "protect seller." That's pro-YOU!

CHAPTER 12

Managing the Property and the Tenant

It's amazing to me how many people will pay an option fee and then walk away a few months later – knowing that they have just forfeited their fees. It is equally amazing to me how many people will try to get their option fees back, even though they are non-refundable.

The option fees paid are for the *right and privilege* to purchase a home. Whether or not the optionee (tenant-buyer) meets the terms of the option is up to them. My goal is to get people to buy and I'll do whatever I can to help them, but I can't make them responsible. I can't make them close on the home either. Approximately half of my tenants ever get to the closing table, and some will walk away from their option fees after only a few months of tenancy. If they forfeit their rights, that's their choice, not yours, but some buyers will try to get that option back in many sneaky ways.

One of the smallest houses I ever lease optioned was in Michigan. It was approximately 700 square feet. It had what is called a "Michigan basement" (kind of like a tall cellar – not something you would finish off as living space). I leased it to a man named Arnold. He and his wife actually moved from a larger house into this little one. You might say that Arnold was like a customer because this was at least the third home I'd leased to him, but he was a good renter, always paying his bills on time. However, it wasn't but two weeks into the rental when I got the phone call with the four dreaded words, "We got a problem." I braced myself and asked "What's the problem?"

Arnold replied, "There's a snake in the house.

I asked, "What kind of snake?"

Arnold said, "A *big* snake - like a boa or python. We found stool samples in the basement and took them to the pet store and that's what he said they told us."

Arnold and his wife now wanted their option fee back and said they were immediately going to move out. He asked me, "Wendy, do you know of any snakes in this house?"

I said, "Arnold, hold on just a moment." I put him on hold and thought about it for a moment and then it began to come back to me that the previous owner, a big burly guy with a lot of tattoos, had snakes. I was a little fuzzy on it because I hadn't been out to the house -- my office manager, Amie, had done most of the visits to that home. I turned to Amie and asked, "Did the previous owner by any chance have snakes?"

She said, "Oh yes, don't you remember? He had cages full of them in the basement. And on the day that we went to close and do the walk-though, I noticed that one of the big cages was empty so I asked him where that snake was and he said he gave it away," she said. We both fell on the floor laughing hysterically. We had never heard of such a thing in all of our years of real estate. A big snake loose in a house. Understandably, it was not so funny to the tenant.

We had no idea where to start. We had dealt with leaking roofs, flooded basements, broken furnaces, frozen pipes, anything else, but BIG snakes? We don't have those in Michigan!

I got back on the phone with Arnold and said, "Well, there's a chance there could be a snake in the house. Let me call the previous owner and see if he knows anything about the snake. I'll call you back."

Do you know how hard it is to find a snake expert in Michigan? I called animal experts, the zoo, pet shops, animal control, exterminators, and I couldn't get help on the situation. I had my handymen go into the house, crawl through everything including the attic in an attempt to find the snake. They could not find a snake.

In the mean time the tenant called and said they had found someone that went into the home and saw the snake's tail go up into the wall from the crawl space in the basement. They also told us they were moving out. I then received a call from their attorney asking for their option fee back. I discussed it with their attorney and several of my friends and the consensus from my friends was they would not live with a snake either. I told the attorney when I found the snake I would gladly return the option fee.

After many more weeks of searching, we finally found a guy whom I nicknamed "Mr. Outback" because he was willing to handle any type of critter situation.

Mr. Outback said, "Look, I've got this glue that's $100 per gallon, and I'm going to put it onto a plywood board and put the board in the basement. When the snake crawls across it, he'll get stuck and we'll have him!"

I let him put the board in, but, doubting the success of this method. I also called the attorney back and said, "I'll tell you what: if you can get sworn affidavits from the people who examined the stool samples and from the people who saw the tail go up into the wall, I'll refund the option fee."

I never heard from the attorney or Arnold again.

In the meantime my partner said, "Sell that house."

The house went back on the market, but I forgot that glue board was in the basement. A Realtor® named Susan was showing the house. She went into the basement and I had forgotten about the glue board. My cell phone rang as she had stepped onto the glue board. "Wendy? What is my foot stuck to in the basement?"

I said, "Oh, that's just the glue board to catch the big snake in the house!"

Susan screamed, and I couldn't stop laughing. I said, "I'll pay for your shoes!" The house did sell not long afterwards, and I wrote on the seller's disclosure where it asks "history of infestation" I answered "None – Confirmed".

I think what may have happened in this case is that Arnold and his wife didn't like the smaller home. When the neighbors told them about the previous owner's snakes, they began to imagine noises in the walls. Regardless, with no snake there was no refund. I could have gone after the rest of the rental agreement also, but we sold the home, so I did not press charges for the rest of the rental agreement. It is amazing what people will do to get out of an agreement.

Wendy's Lesson

Option Fees are **NOT REFUNDABLE** – even though some people will try to get them back. They might make up stories to get their option fees back.

Commitments to the Tenants

If you have tenants in your home, you have certain responsibilities to them. Take care of the house, make sure it's livable, keep open lines of communication. You have to view it as if your sellers and your tenants are your customers. I'm tougher on the tenants because they screw up deals more often, and that's not really an issue with the sellers, but I still always keep my end of the bargain.

Make sure that you're keeping your Realtors®, lenders and others informed at all times, and that they know where to reach you if they have questions. Communication is key!

Protecting Your Privacy with Tenants

In general, you do not want your tenants to know where you live, so either have their rent come to an office or to a post office box. In case a deal goes sour and you have to evict the tenant, you don't want a disgruntled, grudge-bearing tenant showing up on your doorstep. You have to protect yourself and your family. I don't give my tenants my home phone, and that number is unlisted. I would only give them my office or my cell phone.

Who is Responsible for Repairs?

One of the benefits of the lease option is maintenance – the tenant does it all! My lease option with the tenant says that the tenant is responsible for all maintenance major and minor. However, if I end up having to do anything for repairs, I'm going to add that to the purchase price at closing. Let them think through their own possibilities first, but if they still don't know what to do, then you send your own maintenance people and add the cost to the purchase price.

For example, if the tenant's heat goes out in the middle of a Michigan winter, it's crucial to get that fixed. Heat is necessary. On the other hand, if the air conditioning goes out in the summer, it's unpleasant but livable. Do not make your tenant unduly fix too much, because if you treat the tenant like an owner then the court may treat you like a seller – in which case the tenant can say that they've put so many dollars into the property, etc. Then the court may make you go through a forfeiture or a foreclosure versus an eviction, which in most states is more expensive and much more difficult.

In a buyer's market you can put more of the responsibility of maintenance on the seller (Chapter 5 on negotiations). In a seller's market, I don't want them to do anything but to be free and clear of that issue. However, I have to approve in writing of any improvements my tenants do.

Keep a copy of any letter or maintenance regarding the tenant's house. When a tenant calls, we record what was said and what our response was, and it goes in their folder. The same goes for maintenance. We track everything. If the roof leaks and someone slips and falls, accurate files will suddenly become very important!

Transition Between Seller Moving Out and Tenant Moving In

Always assume that the tenant won't buy. Otherwise it's like the proverbial "counting your chickens before they hatch."

Therefore, always have complete documentation of everything regarding a tenant moving in. Probably your most important thing will be to have a video-taped walk-through check-in and check-out with the tenant. It is important that you show them on tape verbally acknowledging the condition of everything, whether good or bad (and hopefully not too much bad – but maybe they'll point out something that you somehow overlooked. If so, fix it immediately!). This is in order to protect yourself with documentation of the condition of the house – documentation that they have signed. The tenant always thinks they're going to buy, but things happen, and a checklist protects you and them. If the window wasn't broken at the time of move-in but is when they move out, you will have video evidence if you need to take them to court and sue for any damages.

After the seller has moved out, make sure it's ready for the tenant. This includes the following steps:

1. Carpets are cleaned if needed (perhaps the seller will do this, but if they don't, you need to make sure it happens).
2. New paint
3. Dings fixed
4. Kitchen and bathrooms cleaned, re-grouted as necessary.
5. Kitchen cupboards cleaned out
6. All appliances left behind are clean and in good working order
7. Check in/checkout sheet that you need to go through with tenant – have them check the condition of everything and sign. Take pictures at the same time or even video tape the walk through for future reference, if needed.
8. Keep track of the title during transition especially if you're not making the mortgage payment, and especially if it's a long-term contract. You want to make sure the title stays clean and clear. Run the title work occasionally if you feel like there could be something going on with the seller or with the company they work for… it's just good to keep the title work current.

Maintenance On the Properties

Although my option agreements state that the tenant is responsible for all maintenance, it is still important to keep the place habitable and treat them like a tenant. If you treat them like an owner, a judge might also treat them like an owner which will nullify the option.

1. Always change the locks from the previous tenant – if you don't change them and someone still has a key, you could open yourself to serious liability.
2. Clean the carpets.
3. Repair any paint problems.
4. Make it habitable.

A Good Buyer Turned Bad

Unfortunately, this business is not all perfect. There are times when you will have a tenant that you think is great. You are sure they will exercise their option. They have paid on time, taken care of improvements/repairs, and been nice in all dealings. Then it happens: You either don't hear from them (no rent) or they start to make things difficult with repairs, etc. In any case, they were a good tenant and now are bad. I recommend trying to work things out on the phone first. If this does not resolve the situation, then put things into writing. If you have a problem with a tenant that can't be resolved over the phone or in writing, then you must go to the next step: eviction and the revoking of their option.

In order for you to do this they must violate a part of the rental agreement. It is for this reason I use option contracts that are subject to the rental agreement being followed. I also include in my option contract this statement: "If any rental or option payment is made 10 days or more late, then this option can be declared null and void by Optionor". It is usually advised to revoke an option in writing before you evict a tenant. This is only a matter of one or two days added to the process. Once you revoke their option, you can start the eviction, as there is no option agreement in place at that time. In most parts of the country revoking an option agreement is not necessary to evict someone, however, it is the safest way.

To revoke an option you can send the tenant a letter via first class mail and certified mail – both containing the information that the option has been revoked. The certified notice is the one you want them to receive and sign for, but if they don't you had sent it first class also. I use this for extra precaution. When you send the revocation letter, you should indicate why you are revoking their option. You might want to attach a copy of their option agreement and highlight the area you are utilizing to revoke their option contract. The letter can be something as simple as this:

Dear Joe, *Date*

Attached is a copy of the option agreement you signed. Your rent is now 15 days overdue and is a violation of the option agreement. You have been late many other times. We are now voiding your option agreement. Please be advised that you no longer have the right to buy this home.

Sincerely,
Wendy Patton – member
Wendy Patton's LLC

Also, if you want to allow them to reinstate their option you can state that in this letter. For example: add this to the end of the above letter:

If you want to reinstate your option, you will need to remit the amount of $$$$ currently due, by MM/DD/YY.

I would recommend this statement if you really do want to work it out with the tenants. Remember to try other softer ways to work it out first; this letter should be a last resort. If this is used too soon in the negotiations, then the buyer can be ticked off to the point of no return.

The best advice I can give on late payers is to start eviction as soon as possible. My office starts to evict when rent is five days late. From over twenty years in this business, I can tell you that tenants lie! You will want to believe them and want to work with them. It will be harder for some of you than others. It was always hard for me, because I have a soft heart. I want to believe people and I do until they prove me wrong. Unfortunately, I have been burned many times from deceit and promises that could not be kept. There is one thing to remember and I hope this helps you be firm on this policy:

Wendy's Advice on Accepting Sob Stories

If the tenant doesn't pay their rent – you are paying it for them.

If you are ok with that, then you can listen to all the sob stories you want, however, most of us can't afford to carry another family. If you don't like playing the "heavy," you can also have your partner/spouse sign the contracts and you and be “the manager.” The tenant doesn’t know you are the owner also. They only think you manage the home. This way when they don’t pay and give you a sob story you can be the good guy. Example: Tenant hasn’t paid rent due to husband being laid off, wife is pregnant, it is December and very cold outside, and it is almost Christmas. You can say, “Boy I really feel for you. I understand this must be a hard time for you. I would let you stay, but I have to start to evict you, or I could lose my job. The owner is very strict on this and really is tight on cash, too. He/She really needs you to pay soon. Do you think you can do it?” This is what you might call good cop/bad cop.

A special note about receiving payments that are post-marked with a Pitney Bowes-type office postage machine: the dates can be changed manually. A tenant can tell you, “I sent you the check,” and you’ll get it maybe several days late with a Pitney Bowes metered stamp that precedes the due date. I tell my tenants that their payment has to be stamped **by the post office** and not a Pitney Bowes machine because of the potential for deceit. When I was first starting out, I didn’t realize that the dates could be changed and I got burned a few times until I got smart.

Of course, you don’t want to have late payments from your tenants, and you want to lay out the ground rules up-front about late fees. However, tenants can feel intimidated to call their landlord with even a legitimate excuse about why the rent is late. It is important, therefore, to keep a rapport with the tenant as to facilitate a comfort zone and open communication. Be friendly but not friends – at least not until the option is exercised. It’s similar to a parent-child relationship. The parent is not the child’s best friend. The parent is the parent, and the landlord is the landlord, and being a landlord is a business. If the tenant doesn’t pay the rent and you don’t do anything about it, you will have to pay their rent – and that’s not a way to run a business.

If you have an arrangement with your tenants that their rent is always due on the first day of the month and you don’t get it, call them immediately or send a notice: “Is your Rent going to be late? Call in with one of these numbers, so we will know why.” When your tenant first moves in, you can give them a list of the most famous excuses you’ve had for rent being late. It’s a little humor but at the same time lets them know you’re heard it all before and that you’ll be watching. It also shows there is a serious side to paying rent on time. You can add to your own list as you learn through the years. You won’t believe the excuses you will hear.

Wendy’s Tip

At the very least, tenant issues provide a great wealth of learning experience, and many times a good laugh! Learn to smile at the stories, it helps relieve the stress.

Collections Procedures

Each state has different collection procedures and abilities. In Michigan I can garnish bank accounts, wages, tax refunds, etc., even “Execution Against Properties” which is going after personal property to resell and claim the money. Use a collection service, but be aware that the collection company will take 40-60%.

Tips to Increase Profits

- Sometimes it pays off to find the tenants before you find the house!!! Line up a bunch of potential tenants, then go find the homes that will fit them in their price range and in their area. – especially good in a buyer's market.

- Charge for late rent. My rental agreements say that I will charge $5 to $25 per day, and I do enforce that.

- Charge court costs, state fees, legal fees, whatever your state will allow you to charge.

- Define "on time" to your tenants

- I always pay the water bills myself, then bill the clients for them. The reason I pay them is to make sure they are paid on time. Otherwise my city can put a lien on the property if it were left up to the tenant and the tenant didn't pay. Check your state out to see if this applies. In many states it is not a lien on the home.

- Money orders and certified funds are not always good because a tenant can do a stop payment on them so know that they can bounce! (Go ahead and ask I how know ☺. If you lose it, they'll reissue it because you've put a stop payment on it.

- Enforce your maintenance co-pays.

- One technique is to call the bank when you get a check and see if that check is good. They won't tell you how much is in the account but they will tell you if it's good or not.

  If it's not good, call back a few hours later and have a lower number and ask if a check for that amount is good. Say, if the first was $1,000 and not good, maybe the second call is for $800. If that's good, then you know that the account has between $800 to $1,000 in it. So then go and deposit $200 into their account, and then cash the $1,000 check. Of course you will bill back the $200, and the tenant might be very angry, but that's tough. Yes it is sneaky, but heck they owe you the money. You MUST call and make sure the check is good before you try to cash it because the bank will only submit the check twice.

  With me you get the chance to use personal checks UNTIL one bounces. Thereafter they all must be certified funds or a cashier's check.

Moving a Tenant Out When They Decide Not to Exercise

If the tenant decides not to buy the property, then you want to go through the property with them and check them out.

If you had a security deposit with the tenant, keep in mind that in most states a security deposit cannot be used to cover normal wear and tear on the property. Normally with an option I don't have a security deposit because I want their money tied up in option (non-refundable) as opposed to a security deposit (refundable), but there is good argument to have money tied up in security deposit because then it looks more like a rental agreement. Of course, if they have animals you might also want to charge a security deposit for that. In any rental agreement, if the security deposit isn't enough to cover damages, you would have to sue the tenant to get any additional amount.

Nikon Drive Property

I lease optioned this property to a real estate attorney's daughter. She wanted her dad to review the contracts. I don't mind at all if an attorney reviews my contracts because I'm not going to change them much. The dad called me after he reviewed the contracts and said, "I'm not changing one thing."

I said something like, "Oh no, the contracts must not be very good?"

He said, "No, you don't understand. My daughter made her bed and she can lie in it. She got the bad credit herself; she can fix it. Your contracts are tough, but they're fair. If she doesn't do her part, she can lose her money. I'm not bailing her out anymore." Thankfully the daughter made her payments and ended up buying the house. I made $35,000 on the deal. I saw the daughter three years after she closed on the home. She ran up to me and hugged me and thanked me for her home. She had recently sold it and made over $40,000 herself. She had two children and needed a larger home. This is a true win/win/win!

CHAPTER 13

The Simultaneous Closing –The Big Payday

Closing – The BIG Payday!

This is when it all comes together! This is payday in real estate investing. If you have been working with your tenant-buyer from the beginning and keeping them in touch with a mortgage broker, you will know when they are ready to purchase your home. They are finally ready to close. If they want to use a mortgage broker of their own choosing, that is fine. Just find out who it is and keep in touch with them, so that you will know where they stand on getting their mortgage completed.

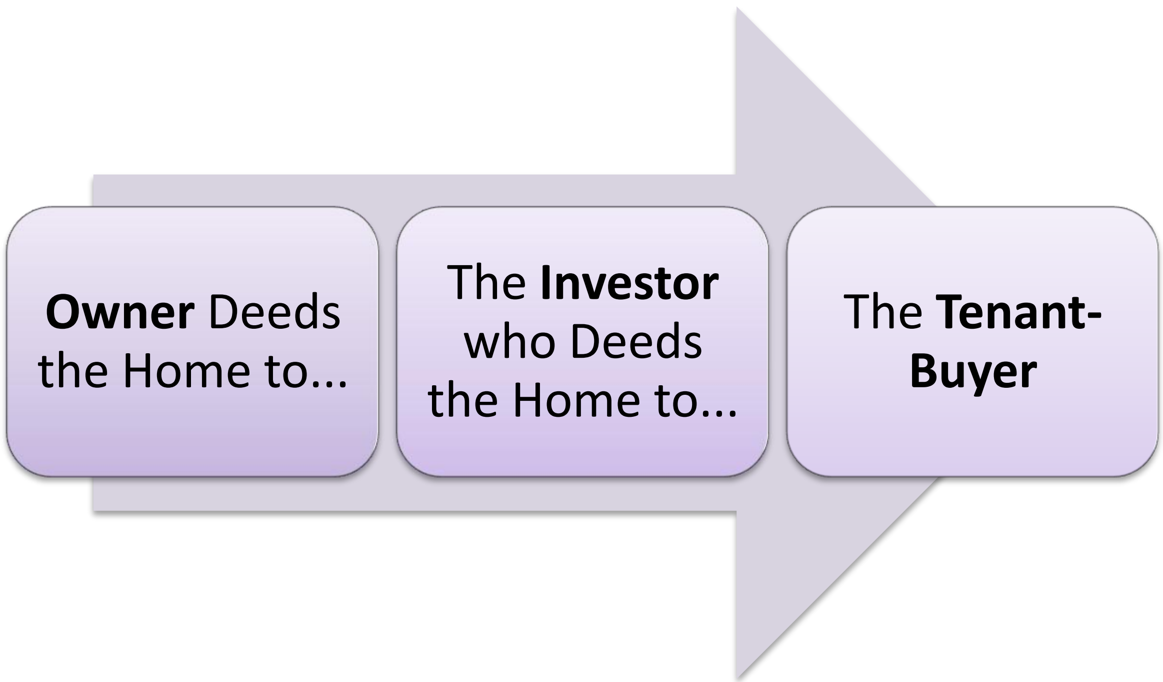
Although the paperwork was signed many months earlier, often the mortgage lender may want you to change something on the contracts in order to get the mortgage approved. For example, the buyer may need more money for closing costs, so the lender may ask if you are willing to pay for some closing costs if you increase the price of the home by the same amount. I am always willing to do this, as long as the home can appraise for the new amount. Appraisals have been a bit more difficult lately, so this might become an issue. A way to avoid this is to make sure you set up the lease option right from the beginning. You need to make sure that what your tenant buyer puts down and option credits you give them each month, will be enough to close at the end of the option period (based on the current mortgages available in the market place). The lender will work with you on these numbers and changes, but they do happen frequently. I am always willing to work with them as long as the changes are fair for all parties involved.

I have also been willing to hold a second mortgage for the buyer. For example, the buyer is purchasing the home for $200,000 and they gave me $4,000 option fee, therefore they owe me $196,000 and possibly less with option credits for paying on time, etc, however, the lender wants to them to have five percent plus closing costs into the home, and they don't have any more money to put down. They really need an additional $10,000 to close this home. I might be willing to hold a second mortgage for these buyers for the $10,000 if I believe the home is worth the mortgage and I believe the people will pay me on the mortgage. I would then get all of my profits out of the home at the closing except the $10,000, which I would get out over time with payments on the second mortgage. Many times on the second mortgage I do a one or a two year balloon so I get paid off fairly quickly. They would have to refinance the home in that time period and pay me off. Note however, that second mortgages MUST be on the HUD statement and known to all parties. Our current mortgage climate may not allow for this, so beware that they might not be so easy to do.

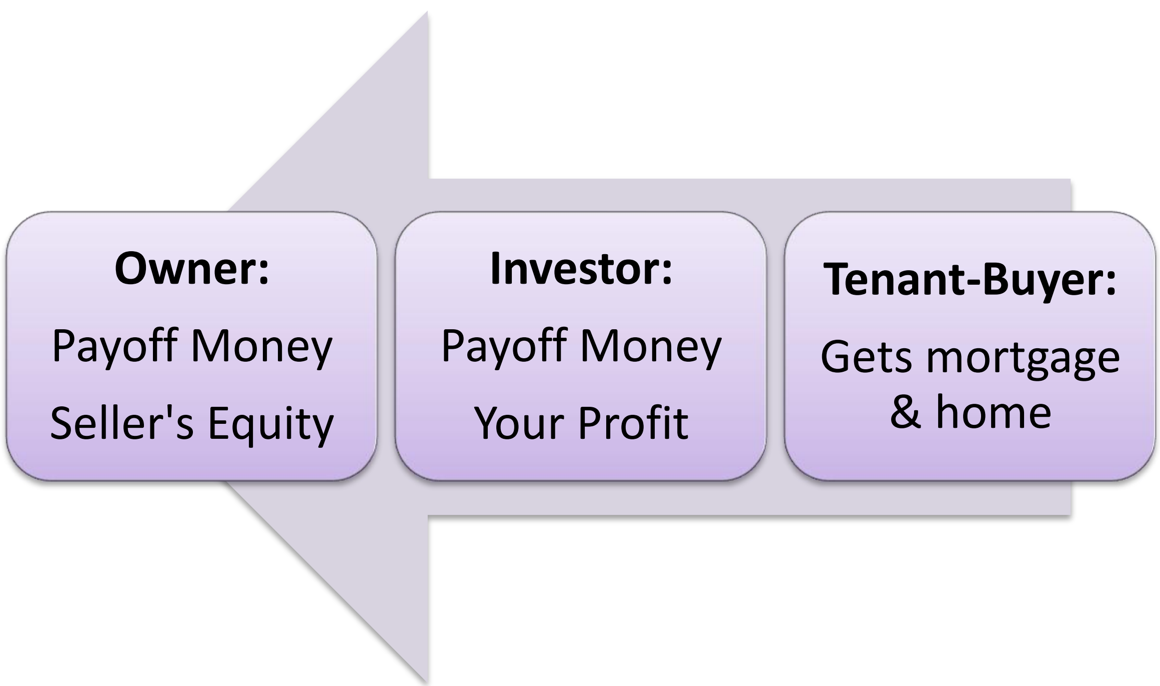
A simultaneous or double-closing is when there are two closing on the same home at the same time or the same day. It is sold and bought the same day. It used to be that we, as the investor, didn't need to bring money to the closing table, but now that is not possible in any state. You must have the funds to buy before you can sell. You can get funds for a twenty-four to forty-eight hour time period, called **transactional funding**. It will cost you a couple of percentage points, but it will get the deal closed for you. This is one way to handle this situation.

The other way is to get the seller to sell directly to the buyer and you put a lien on their home for the amount of your profit. All parties still get what they want, but it does take a little more creativity on your part. There are ways around most everything, when we use our creative minds. This last idea also helps with "seasoning" requirements set up by many lenders today.

Typical Example of How the Deed Flows



Typical Example of How the Money Flows



Find out when the buyer is going to close and keep in communication with the seller about it. Go back and forth on it until finally you get it down to the exact day and the exact hour. You should be the coordinator, not anyone else. You have to make sure all the pieces fall into place. You coordinate the tenant making arrangements with the mortgage company. Make sure the buyer, the title company/attorney and the mortgage company are all on the same page. I recommend you reconfirm each party the day before. It would be a shame for the deal to fall through due to a scheduling oversight.

The mortgage lender only sees one side of the transaction – the side between the investor and the buyer. To the lender, I am the seller. To the seller I am the buyer. The title company sees both parts. Make sure when you are coordinating with the title company or attorney's office that they know both sides of the transaction. They will need the paperwork on both sides. To them it is two files.

The mortgage lender will need copies of the contracts, a payoff letter, and copies of cancelled checks. From the very beginning, ask the tenant to keep copies of their cancelled checks. With the banking industry changing and us not receiving our checks back, they might have to order these, but I keep a record of all of their checks -- the check number and date paid. I also put a copy of their check in their folder. They may not keep records like I do, so I can help them gather this information quickly. For most lenders, if they want to do a lease option refinance type of program, they will need twelve months of cancelled checks, or proof of payments. A letter from me alone is not enough. A bank cancelled check is real proof or a bank statement showing their cancelled check is what the lender will require.

I usually don't like my buyers and sellers to meet (unless it is necessary due to seasoning issues with the mortgage for my buyer). Though intellectually, each of them know I am making a profit and each of them know I am a real estate investor, to put a dollar amount in front of them can destroy their enthusiasm. In each of these real estate deals, they are a win/win/win for each person involved, but change the scenario to put us all at the same closing table. Have the seller and buyer see me get my check for $42,400. Now, their joy is robbed. They are not as happy about the deal they each received when they know exactly how much I am getting. The atmosphere of the room changes quickly. I would not want to change the way they each feel about the deal and therefore I would not ever put them together again. This is from experience!

Usually you will close with the seller and buyer at almost the same time if you are using transactional funding. You can find transactional funding at http://www.WendyPattonFunding.com if you do not have a resource for this service.

Example of a payoff letter for the lender:

To Whom It May Concern: Date

The payoff for 123 XYZ Street is:

Price	$200,000
Less Option fee paid on XX/XX/XX	***-$ 5,000***
Additional option credits earned	-$ 1,100
Balance Due as of XX/XX/XX	$193,900

Please feel free to call me for any questions.
Sincerely,

Wendy Patton
Wendy Patton, LLC - Member
(222)333-4444

(Add anything else they owe such as any repairs during the option period or outstanding utilities, etc. Don't forget to get it on the payoff letter now.)

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Chapter 14

Advanced Concepts and Strategies for Selling on Lease Options

I once bought a parcel of property on a land contract. The property had splitable acres in a town near me which was fairly rare. One part of the property needed development and the other part had a house. The seller of the house was an older lady who had lived there for 30 years. Because the house needed some work, I lease optioned it as a handyman special. Along came Steve who was a licensed builder. Because he was a licensed builder, I had him sign all the contracts under her personal name and his company name.

Wendy's Advice

When signing contracts always have the tenant-buyer sign personally and under their company name if they have one – especially on the rental agreement.

Also have all parties over the age of 18 sign the rental agreement. This puts each person and their company liable for the debt if the tenant-buyer does not pay.

For Steve, this seemed like the perfect house. There wasn't anything in it that needed fixing that he wouldn't be able to tackle or have the resources with other contractors to tackle. It wasn't too far into the renovations, however, that Steve called me and said, "We got a problem – this house has been in a fire."

I was unaware of any fire, so naturally my first response was to call the seller and ask if she knew anything about a fire. The seller confirmed that while she lived there that there had never been a fire. Now because the house was built in the 20's or 30's, there was a possibility that anything could have happened to it, but she didn't know of it and my inspectors and I didn't know of it. Steve said, "Wendy, I can't even believe the roof is standing because all the rafters are completely charred all the way up and through the decking."

I asked him what it would cost to repair, and he said $3,500 in materials. I offered to give him $3,500 off the purchase price when he exercised the contract. Now, this was advertised as a handyman special, so I didn't cheat him or lie to him. How could I know what was up under the plaster?

Everything seemed to go smoothly for months, he was making repairs and improvements, and I was sure he was going to exercise. Month seventeen came and I asked him if he'd been speaking to the lender and if he was going to get a mortgage. He said he had a little glitch in his credit and so I asked if he wanted to extend for another six months. I didn't really have a problem with this because he'd been paying perfectly, but he said, "No, I'm moving next month. I don't like all this development happening around me."

Steve knew about the development when he moved in and it was documented in the contracts that he signed. He moved out and sued me for the option money he had put down in the beginning.

Being sued is scary and nerve wracking for most people. I don't like it, but I have been through it a handful of times. It's inevitable, and all the more reason to keep excellent records on every little thing that happens with each house, each conversation, each mailing, every document, etc.

In court Steve told the judge that there were many problems with the home and he showed the judge many pictures of the home and of the fire damage. The judge asked if he thought I knew about the fire. He responded, "No, I couldn't tell either, it was covered in plaster". The judge asked me. I said I did not know and that I did offer to pay the $3,500 to fix it. The judge looked over our contracts very briefly, and noted where it said the home was sold "AS IS" and that it was a handyman special and that he had had the home inspected. The judge pulled her glassed down to her nose, pointed to a paragraph in my contract and said to Steve, "Wendy did not have to offer to pay anything for the roof, she was more than fair. So, Sir, I have just one question for you. What part of, 'This option fee is NON-REFUNDABLE' do you not understand? Case dismissed. Next." Steve got up and stomped out of there very mad!

Advanced Selling Strategies for Lease Options

1) Handyman Specials

Handyman specials are homes that are less than perfect and require sweat equity to bring them up to a new level of respectability. There can be a lot of money to be made in a handyman special. The tenant-buyer's overall purchase price, or option fee required, is going to be lower for the privilege of doing the work themselves. I actually can't provide enough homes for people out there who want this situation. This technique will work in most areas of the country except in areas where the city requires certification or landlord licensing. They don't work in those areas because the city won't allow homes that aren't perfectly up to code to be rented, and sometimes these homes might just need paint or a few items, but sometimes they may need some major items also. In the areas where the city doesn't require inspections or certifications, it can be a great way to liquidate your properties.

Tenants have a perceived value in the fact that they will do the sweat equity. You'll make just as much money and you won't have to go over budget on doing your own rehabbing. One word of caution: make sure the home is habitable. It must be able to be lived in, or you will have problems if the tenant-buyer doesn't pay and decides to fight you on rent or their option. Any judge will expect the landlord to provide a habitable home for their tenant. The tenant-buyer is going to love you because you are giving them the American dream: a nice fixer-upper.

2) Section 8

Section 8 is a rental-assistance program funded by the Federal Housing and Urban Development Department (HUD), which gives approved tenants financial assistance by paying a portion of the rent directly to the landlord. Section 8 now has a new program for lease options.

Section 8 doesn't control the particulars of how the lease option is set up, but will make the monthly payments on it. After the lease option is started, they will help the tenant-buyer get a mortgage that will convert the lease option to a purchase. It's not for every Section 8 tenant but for a select few that qualify. Talk with your local Section 8 administrator and have them come in and talk to your real estate or investor group so that you can have all the current information.

As a landlord I love Section 8, because the payments, or most of them, come directly to me from the state.

3) Ads for Soft Rental Markets

In soft rental markets there will be many rentals and not many good tenants. In order to get a good tenant into your home you will need to make your rental ads stand out. The ad must contain something that looks better than the competition's ads. One idea that I have used is to offer a rent of several hundred dollars lower than I actually intend to rent it for. When the applicants come to the home, I screen them to see if they can afford the extra $200 per month. If so, I offer them 50 percent on the additional $200. It will make sense in a minute—keep reading.

I might say, "You, really like this home, don't you? And you want to buy it, right?" Of course I know they do. "How would you like to make 50 percent on your money?" When they say yes, then I offer to give them a $300 credit to buy the home if they pay an extra $200 per month. Now I am getting my $200 more per month, which is what I originally wanted, but I advertised it at $200 per month less to generate the leads. Yes, it does cost me $3,600 in option credits for the entire year if they purchase, but I rented the home. If they don't purchase the home, I received my entire rental amount. This is a small amount to pay to get someone in during a slow market.

Strategies for Reducing Your Taxes

Many people worry about paying Uncle Sam. How would you like to have to worry about getting into a lower tax bracket because you are making too much money with lease options? When you have been investing for some time and get your pipeline filled with deals, your income will increase and you will need to begin being creative on ways to save on taxes when you sell. You can keep your properties forever, but if and when you sell there are tax issues. There are some things that I have done to reduce taxes for myself.

Exercise Your Option and Hold for Another Twelve Months

If you are in a higher tax bracket, you might want to consider exercising your lease options with your seller prior to your tenant-buyers exercising their options. If you do a simultaneous closing, it is considered a short-term capital gain. You only owned it for one day. You are taxed at your normal income rate. You can sell your option by assigning it. If you have held it for more than twelve months, it is long-term capital gain, taxed at a much lower rate. Unfortunately, if you assign your option, the profits are not nearly as good as selling it to a tenant-buyer, and very few tenant-buyers can pay an entire assignment fee to get you the profit you would receive if they were to purchase it outright. Therefore, if taxes or high tax brackets are an issue for you, consider exercising after the twelve months of payments to the seller (treated as the refinance so you don't have to put down cash out of pocket either) and then make sure your tenant-buyer doesn't close for another twelve months. This would give you long-term capital gains on the ownership of the property and give you a much better tax rate on the profit.

CHAPTER 15

Business Organization for Lease Option Investments

You might be thinking, "I have a few properties, and keeping track of what's going on isn't difficult with some files on my desk" – but apply that thinking to 175 active properties in various stages of buying/selling, renters paying late, evictions, rehabs, and you've got an administrative nightmare if you don't have systems in place.

Whether you have only a few properties or many, you might as well set up your business as if you're planning for many properties – that way you're already in the groove for expansion.

Color Coding Your Files

Have a file cabinet dedicated (or maybe just one of the drawers to start) to your properties. I keep my files in alphabetical order by property address, not by seller or tenant. Each property has two files. How you color code your files is up to you, but I use green labels for the seller (think green for money!), and red labels for the tenant-buyer. When I open my file drawers, it's like Christmas! My folders are half-tab which means the tab goes half way across the top of the folder. It has been easier for me dealing with two tabs and one color is always on the right and the other color on the left.

Seller Folder

The seller folder holds all the documents that you signed with the seller – the pro-buyer contracts. If you own the property on a subject-to or a mortgage, it would contain all of the mortgage or subject-to documents. It also contains any correspondence with that seller. This folder would also contain any information about the home such as title work that was done, surveys, inspections, etc.

Tenant-Buyer Folder

The buyer folder holds all of the pro-seller contracts. It also holds all of the correspondence with the buyer, original application, credit report, copies of payments, all bills, maintenance records, all correspondence, and a CD with digital pictures of the house.

This folder may even contain a digital video recording of a walk-though of the property with the tenant to show the condition of the home when they move in. Keep a copy of each check they write, any water/sewer bills, and other bills that you have sent them. You will need their check copies for when they get their mortgage. These will be needed to prove that each payment was made and when. They will need to get their cleared copies from the bank, but your copies will help them with check numbers to request from their bank.

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This folder should also be used to keep track of any correspondence from the tenant. Anytime the tenant calls we will record the call on a piece of paper, what they said, what we said and how we handled the call – if there was anything to be completed. You will want to document everything with the dates and times, and if you sent a maintenance person, who you sent and what they did to fix or not fix the problem. Hopefully, you will never need the documentation, but if you ever do need it, you will have it there. Don't throw it away until years after you have sold the property to them or anyone else. I had a case where a tenant sued me a year after they moved out for a slip and fall case from two and a half years earlier; however, we had all of our documentation, so it never went to court. Keep your records! I would have never even thought they would have tried that or were even upset about that, but they did. They have a certain number of years to still come back and sue you. So hope for the best and plan for the worst.

Software for Your Business

If you only have a few properties, you don't need any special software for keeping track of their information. A simple spreadsheet in Excel will work just fine. However, if you have many properties, you will want to invest in a property management software program. Talk to someone in your real estate investors group or on one of the real estate websites to see what program will meet your current needs.

When it comes to accounting, there are many accounting programs out there. The one my office uses is QuickBooks. It writes our checks, keeps our accounts balanced, and at the end of the year we get itemized reports per property, per expense account, per LLC, whatever we want. All the good accounting programs will do this for you-- the key is to make sure the software can track items by property so that whenever an item is paid or received, it is linked to a particular property. If you are using the appropriate software and have religiously assigned the payments and deposits, you should be able to quickly see a summary and/or detail of all income, expenses, improvements, etc. by property. In QuickBooks, using "Class Tracking" with each class being a particular property, we are able to easily accomplish this. Another advantage to good bookkeeping records is your bill with your accountant will actually be lower because so much of his work is already completed.

Work Orders

When something goes wrong in a home, or when you have work to be completed, you will need a process to track the work. We purchase work order books that have carbon copies from an office supply company. We put the property address on the work order, the tenant's name and number, if occupied, and the problem. We keep one copy for us and we give one to the handyman. The handyman must complete the work order and fill it out with detail of what was completed in order to get paid. He/she brings back in his/her copy to us. We then follow up with the tenant (if occupied) to make sure it was in fact completed. If so, we issue their check. We keep a copy of the work order in the tenant file. The repair cost may later be added to the purchase price, depending on the option contract with the buyer and the extent of the repair. The seller may also be responsible depending on what was negotiated with them.

Tenant Payment Ledger

I set up a tenant payment ledger for each property that is either a rental or an option. Here's an example of what it will look like:

Company Name: (Your Company Name)____	Option Fee____________________
Address: (of rental property)_______________	NSF:____
Tenant Name:__________________________	Lease Dates:___________________________
Home Phone: (of tenant-buyer)_____________	To:_____________________________ _____
Rent: (monthly rent)______________________	From:___________________________ _____
Other Charges: (if applicable)_____________	Water Softener: (amount if applicable)_______
Security Deposit:_______________________	City Water: ____________________________
	City Sewer:___________________________ _

The next section of the ledger is the payment history. Our tenant will have an option fee of $1,500, and their move-in date is November 1, 2XXX. The monthly rent will be $1,095, and there's a quarterly water/sewer bill of $52.50. The credit column is for the tenant payments. The debit column is what the tenant owes, and the balance is a combination of the credit and the debit. It should look like this:

DATE	DESCRIPTIONS	DEBIT (owed)	CREDIT (paid)	BALANCE
11-1-XX	Option Fee	$1500.00		$1500.00
11-1-XX	November rent payment	$1095.00		$2295.00
11-1-XX	Option Fee		$1500.00	$795.00
11-1-XX	November rent payment		$1095.00	$0.00
11-10-XX	Water/sewer	$52.50		$52.50
11-23-XX	Water/sewer payment		$52.50	$0.00

Using a Tenant List

I have created a document showing all of the properties I own, the current tenants, their lease option expiration date and what utilities they are responsible to pay. I also have a column showing me the owner and their address if I have purchased it on a lease option, along with my contract expiration date. This list allows me at a glance to monitor who should be working on their financing at this time instead of digging through files to keep track. I can always stay ahead by checking my list on a regular basis and getting my tenants to a mortgage broker several months before their contract expires.

Sample Tenant List:

Property	Company	Owner info	Contract End	Tenant	Lease End	Rent	Utilities	Misc. Info
123 Flint	MR Ltd.	Sally Harris (234)222 -2343	XX /05/ 31	John & Jane Smith (333) 333- 4444	XX/03 /31	$995	Twp Water/ sewer	Lease opt.
123 Genoa	MR Ltd.	Joe & Jane Smith (222)342 -4444	XX /02/ 28	Cary & Jen Edwards (333) 333- 4444	XX/03 /31	$1,195	Well, septic Softener	Lease opt.
123 Hill	MR Ltd	Sally Seller (111)222 -2222	XX /3/3 1	Leroy DuBois (333) 333- 4444	XX/04 /30	$1595	Sewer /well	Lease opt.
123 Hunt	Mill Ltd.	June Taylor 123 Bliss Street Ann Arbor 48123 (333) 333- 4444	05/ 07/ 12	Bradford Shue (333) 444- 3333	XX/05 /31	$1,795	Township Water/sewer	Lease Opt.

Keeping Necessary Documents On Hand

It is extremely important to keep documents in your office that you will be using on a regular basis. Nothing is more annoying than needing a document and finding that you don't have it. Spending time searching online or going to your local office supply store to get it is a waste of your valuable time. For instance, depending on your state, you can download seven-day notice forms and other tenant or legal documents from the state website. Save these documents to Word to enable you to pull them up and tailor them as needed. You may want to create a "document checklist" to make sure that you have what you need and when your supply gets low you can reorder before you run out.

Good Recordkeeping is a Must!

In addition to the two above-mentioned folders, one more file should be used to store every receipt for each property. There are always expenses that the tenant is not responsible for paying (advertising costs, attorney fees, improvements, etc.). In our office, we use legal size folders or large title company envelopes (free from the title company that we use). Each folder or envelope is labeled with the property address and filed in alphabetical order. Every time an invoice or bill is paid for a particular property, a copy of the invoice is filed under the property address. We note the check number and date paid on each invoice. If the tenant is responsible for reimbursing us, a copy of the invoice is also placed in the tenant file. At year end, these receipt files will contain all documentation needed to substantiate all expenses, improvements, etc. for that particular property.

For those items that cannot be associated with a particular property, for instance: general advertising not tied to a particular property ("We Lease Homes," "Office Manager Needed," etc.), postage, office supplies, license fees, or the like, we use a file labeled "General Rentals" and file receipts for those type of expenses in this file.

The last type of file used to document our bookkeeping is a file for each bank account, labeled with the LLC name and "Cancelled Checks." We file all the bank statements and cancelled checks for that LLC in that file.

At year end, all files are moved to storage boxes. Each box is labeled with the LLC name and year. Placed in this box are all the files with the receipts for each property under that LLC as well as the cancelled check/bank statement files for that LLC. This may seem like a lot of paper to store away and some of it may seem redundant (a copy in the tenant file and a copy in the property receipt file), but if you are ever unfortunate enough to go through an audit, everything you need to support your tax filing is in one box, efficiently organized and easy to retrieve. You hope you will never need them, but there are times you will need a copy of a receipt and you certainly want to be able to locate it quickly.

Also, if you were ever to be audited, you want to be able to prove your expenses and income quickly and easily. I have been audited twice and my audits went very well because my records were so easy to find and my records were very clean. The auditors first words when arriving to my office and getting a tour of our records was, "Wow, you are VERY organized!" You don't want to be audited, but if you are, you want someone to respond that way.

When to Hire Someone

At some point you will need to hire someone to help in your business. When your business has grown to the point where you are no longer able to handle all the tenants or bookkeeping or organization necessary to efficiently run your business or you are so busy handling the "little stuff" that you are not spending enough time on the real "money making" end of your business, it is time to get help. The first thing to do is to evaluate your own strengths and weaknesses. Then, hire someone to take over your own weak areas. If you are great with tenants, but lousy at bookkeeping, get a part-time bookkeeper. If you are a lousy organizer, get someone to help with this. Perhaps the only thing you need at first is someone to handle the phones, correspondence and busy work. If you have hired the right person, their responsibilities will grow as your business grows. The important thing is to stay focused on the most important part of your business, which is new finding properties.

Qualities for Hiring Staff

When hiring an office manager or property manager, there are many qualities you should consider; however, there are a few that are the most important I have discovered over the years of being in this business.

We all want the perfect candidate and employee, yet we can't afford to have someone with all the qualities we desire. We must compromise. We must pick qualities that are the most important skills for the job we need accomplished. The rest of the skills will be bonuses. This person will be your right hand person and part of your team; therefore, it is very important that you do select the right person. Here are the skills that I have found to be the most important over the years – and not necessarily in order of importance:

- **Firm**: There are times when a tenant will try to push the limits with being late on rent. You want your assistant to be firm, but pleasant.

- **Pleasant:** Your assistant must be pleasant even when you want to blow up. There are times when I have wanted to lose it with someone on the phone, but my assistant will keep tempers on the level because he/she is not personally involved, so he/she can be non-emotional and pleasant.

- **Detailed**: This person must be able to be very detailed. They will be tracking tenants' rent, late fees, water bills, option fees, correspondence and many other items. Everything must be detailed and documented.

- **Good Follow-Through:** This area is so important as the little details that fall through the cracks can cost you tens of thousands of dollars and lawsuits. Making sure that nothing falls through the cracks is so important; for example, did the gas get turned on at your vacant home in January? In the Michigan area, this is very important, or you might have an ice skating rink in your home! How do I know? I had some follow through problems.

- **Organized**: Following your systems you have in place and your check lists will be very important. Also, making sure that your assistant has things well organized, labeled, filed, etc., so that you can easily find them when you need them will be very important to you.

- **Computer Skills:** It is impossible anymore to not be involved or know computers, so make sure your assistant has computer skills. Basic word processing and spreadsheets are usually the most important parts of property management. Spreadsheets can be taught, but word processing is a MUST.

- **Take Initiative/Work Independently:** Your assistant must be a self-starter. They must know what to do when you are on the road. You will be in and out of the office much of the time, or you will want the ability to be. Make sure you hire someone capable of running things if you are out of town. Can they handle calls? Make decisions? Make good judgment calls? Will they work when you are not there watching them?

My best part-time employees are women that didn't need their jobs; they wanted their jobs. This makes a huge difference in the way they perform at work. They were all professional women who chose to take a few years off to be at home with their children. Once their children became school-aged, they all wanted to return to work part-time. They have excellent skills, enjoy working, but flexibility is their key (sort of like “terms” on a lease options!). This business can offer that.

When someone needs to work, you would think that would be enough motivation. However, if they are not motivated themselves, it is not enough to keep them motivated every day. If someone wants to work, that is enough motivation. If they don’t need the money, but want the job, now there is someone you might want to consider. Now these are all just guidelines, because I have also had several full time employees that did need the jobs that were fantastic also.

Wendy’s Advice

If you are hiring someone part time – you might want to consider someone that doesn’t *need* a job, but instead someone who *wants* a job

In Conclusion – Where Do I Go From Here

Lease Options are an excellent tool to have in your investment pipeline. This eBook was designed to outline the entire process from start to finish in the clearest and easiest terms. So what next?

If you haven’t looked already, I have additional on-line course segments which break down into sections what this eBook covers: Buying on Lease Options, Selling on Lease Options, and Working with Realtors®. All of the forms I refer to in this eBook are included with step-by-step instructions on how to fill them out along with actual calls I have made to buyers and sellers, plus a whole lot more.

I also offer live training classes—both One Day Workshops and a more in depth BootCamps hosted throughout the year. These training classes are very hands-on -- we make calls to buyers, sellers, and Realtors®; we walk through the lease option process, practice role playing -- everything you need to do to leave with your first lead.

The last page of this eBook has a valuable Reference Page which spells out where to reach me, where to check out my national speaking schedule, more free articles, and more.

I honestly believe my success comes from your success so…

LET’S GET GOING!

Resources for the Real Estate Investor

- www.WendyPatton.com
  Wendy Patton's Website which includes articles, her speaking schedule, blogs, and more.

- www.gottlegalplans.com
  PrePaid Legal: For affordable legal assistance with no contract required.

- www.RenttoOwnCreditRepair.com
  A great source for credit repair. Get your tenant-buyer signed up as soon as they sign a contract with you.

- http://www.cpsc.gov/cpscpub/pubs/426.pdf
  Protect your family from lead in your home pamphlet. Must be given to buyers and renters as part of Lead Based Paint Disclosure.

- www.craigslist.org
  A resource for listing your rent-to-own home. Also a good resource for finding free or inexpensive home improvement materials and moving boxes.

- www.craigslist.org/about/FHA#categories
  A state-by-state description of what classes are protected by law from housing discrimination.

- www.familywatchdog.us/default.asp
  Free search for convicted sex offenders by name or location.

- www.freecycle.org
  A good resource for finding free home improvement materials and moving boxes.

- www.hud.gov
  U.S. Department of Housing and Urban Development

A Special Note about Lease Option Deals in Texas

If you want to deal with lease options in Texas I suggest you study House Bill 1823 and Senate Bill 629 to make sure you follow all of their state rules and regulations.