

HOW TO USE  
**CREATIVE FINANCING  
TECHNIQUES**

TO YOUR ADVANTAGE

by Dyches Boddiford



## Why Creative Financing?

Beginning & unsophisticated Real Estate Investors let the bank tell them what they can buy.

- ✘ This doesn't work anymore.
- ✘ And for many investors, it never worked; for example:
  - ✘ Those with too many bank loans already
  - ✘ Poor credit because of foreclosure or bankruptcy
  - ✘ Not enough down payment

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## Why Creative Financing?

*“Using institutional financing is a sign of intellectual inadequacy.”*

Pete Fortunato

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## Why Creative Financing?

Understanding Creative Financing Techniques (CFTs) puts you a cut above your competitors.

Some of the many Benefits:

- ✘ Little or no qualifying
- ✘ Better terms
- ✘ Low or no down payment
- ✘ Lower closing costs
- ✘ Faster closings

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## Why Creative Financing?

In short, Creative Financing Techniques...

***Allow you to make more Deals***

**&**

**Better Deals**

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## Why Learn Right Now?

Today's market is ripe for Creative Financing Techniques!

- ✘ Only 50% of people wanting a loan on real estate can get financing today.
- ✘ If you can buy while prices are down, you can make a mint when values go up.
- ✘ In the meantime, rental rates are projected to increase significantly.
- ✘ Loans are a great investment for your IRAs!
- ✘ And being in hard assets will protect you if there is significant inflation.

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## WHEN TO CONSIDER CFTs

- ✘ Whenever you –
  - ✘ Buy
  - ✘ Sell
  - ✘ Need additional financing
  - ✘ Want to grow your IRA
  - ✘ Work with a Partner (Debt or Equity)

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## Creative Financing Techniques

### As a Seller -

- ✘ Easier/quicker to sell.
- ✘ Can sell for full price & keep more.
- ✘ Installment sale tax treatment for investment properties.
- ✘ Better returns – interest on before-tax dollars.
- ✘ Way to control mortgages currently on property.
- ✘ Way to sell property with a title problem.

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## Creative Financing Techniques

### As a Buyer -

- ✗ Financing built in.
- ✗ Often no credit check/reporting.
- ✗ Often low to no down payment.
- ✗ Quick closing.
- ✗ Favorable terms can be negotiated.
- ✗ Keeps the door open to future negotiations.
- ✗ Seller may have other properties to sell or even money to lend once you prove you pay on time.

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## To Negotiate Financing

- ✗ Be professional - Hone your negotiating skills
- ✗ Be sympathetic - Spend time understanding the other party's needs
- ✗ Don't just be an "Order Taker" - Lead them into understanding why financing could be best for them



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## Negotiating the Financing

### Terms as Seller –

- At least 5% down, preferably 10%
- Market to above Market Interest
- 20 year Amortized w/3-5 year balloon or call
- 5 Days Late, 10% Late Fee
- No Default Notice required
- Payment due each and every month

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## Negotiating the Financing

### Terms as Buyer –

- No money Down
- 0% to under Market Interest
- 30 to 40 year amortization
- No Late Fee
- 30 Day Default Notice
- Substitution of Collateral
- Maybe ability to skip a payment

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## Possibilities

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- Take existing loan subject-to.
- Offer as down payment for Seller financing:
  - Pay Seller 1 year in advance.
  - Put significant money into property.
- Performance note (Seller gets what he wants if property produces as he represents).

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## Possibilities

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- If Buyer offers to put significant money into property and asks for lower down payment, escrow improvement money.
- If Buyer does not have all the down payment you require (5-10% or more), may work rest out over a number of months or use L/O.
- Consider other collateral Buyer may have.

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## Possibilities – Balloons & Calls

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- Definition...
- If a Balloon, give them an extension clause for a pay down of principal.
- With a Call, remember an amount less than full balance can be called.
  - (But if amount is a significant portion of balance, Buyer may need to pay off to get new loan.)

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## WRAP Mortgages

**Wrap Equity**

**Existing 2<sup>nd</sup> Mortgage**

**Existing 1<sup>st</sup> Mortgage**

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## Possibilities – Wrap

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- Wrap existing loan with equity at higher rate.
  - Retain control of underlying loan(s).
  - Make sure Wrap reflects underlying loan terms.
  - Collect total payment from which you pay underlying loan.
  - Great for building wealth in IRA!

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## Example Wrap

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- Sell property for \$150,000
- Take \$7,500 down
- Existing loan of \$120,000 at 7.25%
- Wrap existing loan with remaining \$22,500 equity at 8.5%
- Yield on your Wrap equity is

15.65%!

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## IRA WRAP LOAN EXAMPLE

An investor has found a house that when fixed up will be worth at least \$150,000. The investor has been able to negotiate a purchase price of \$100,000. He has found a \$90,000 loan (owner financing or other) at 12%. The house needs \$5,000 in fix up for paint, carpet, etc.

The investor wants to flip the house and comes to you to borrow the money. You happen to have \$15,000 in your self-directed IRA. You decide it is a good deal.

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## July 29, 2011

National		California	
FICO® Score	APR	FICO® Score	APR
760-850	4.126%	760-850	4.129%
700-759	4.348%	700-759	4.446%
680-699	4.525%	680-699	4.627%
660-679	4.739%	660-679	4.846%
640-659	5.169%	640-659	5.285%
620-639	5.715%	620-639	5.844%

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## Getting 0% Financing

- ✘ You will never get 0% if you don't ask for it!
- ✘ Begin by convincing seller to owner finance.  
Typical reasons:
  - + To get higher price (no closing costs for 3<sup>rd</sup> party loan)
  - + Quick sale
  - + Property may need significant repairs
- ✘ **DO NOT** bring up interest rate in beginning!
- ✘ Then walk through the numbers...

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## Making Financing More Secure

- Minimum 5% down. The more the better...
- Decent credit history
- No more than 1/3 income going to mortgage, taxes & insurance (25% better)
- Total monthly obligations no more than 41% of income
- On same job for 3 years or longer
- Co-signors or Guarantors
- Additional Collateral
- Automatic withdrawals

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## Alternatives to passing Title

- **Lease-Purchase** – Purchase agreement providing an obligation to close on a future date with a lease until closing.
- **Lease-Option** – Option agreement providing the right, but not the obligation to purchase by a future date plus a lease.
- **Land Contract** – A purchase money contract where title is not passed until a later date.
- **Pure Option** – An option agreement providing the right, but not the obligation to purchase by a certain date with no interim control over the property.

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## Alternatives to passing Title

**As a BUYER**

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## Lease-Option

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- ✘ Gives you the ability to “test drive” the property.
- ✘ Unlike lease-purchase, can decide not to buy.
- ✘ Can often get for 3 to 5 year term.
- ✘ Lease deposit & option fee –
  - + Usually less than down payment.
  - + Could be negotiated to be refundable.
- ✘ Lease could be a performance lease.
  - + e.g. – Lease payment 88% of amount collected on sub-lease.

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## Lease-Option

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- Can negotiate portion of lease payment to go toward down payment for purchase.
- Owner still responsible for –
  - Maintenance,
  - Property taxes &
  - Insurance
- Or triple-net lease for lower lease payment
- Secure option in land records

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## Land Contract

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- Considered sale by IRS on day signed.
- Gives owner comfort in holding title.
- But use title-holding trust with trustee with whom both you and seller feel comfortable.

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## Pure Option

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- Advanced – to get low price, may give owner option to buy back for period of time.
- Secure option in land records.
- Can pay one option premium for full term or a renewal fee per period.
- Owner still collects any rent and manages the property.
- Owner has obligation to sell to you during option term if you exercise option.

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## Alternatives to passing Title

**As a SELLER**

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## Lease-Purchase

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- ✘ Gives you chance to see how Buyer does in paying and handling property.
- ✘ Down payment should be 10% (no less than 5%)
  - Term based on your objectives.
  - Get lease deposit & earnest money. Both apply upon purchase by buyer.
- ✘ For investor buyer, lease should provide right to sub-lease to lower liability exposure.

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## Lease-Purchase

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- Determine if any portion of lease payment to go toward down payment.
- Negotiate triple-net lease – Buyer then responsible for property taxes, insurance and maintenance.
- Make owner financing on purchase contingent on making all payments on time under lease.

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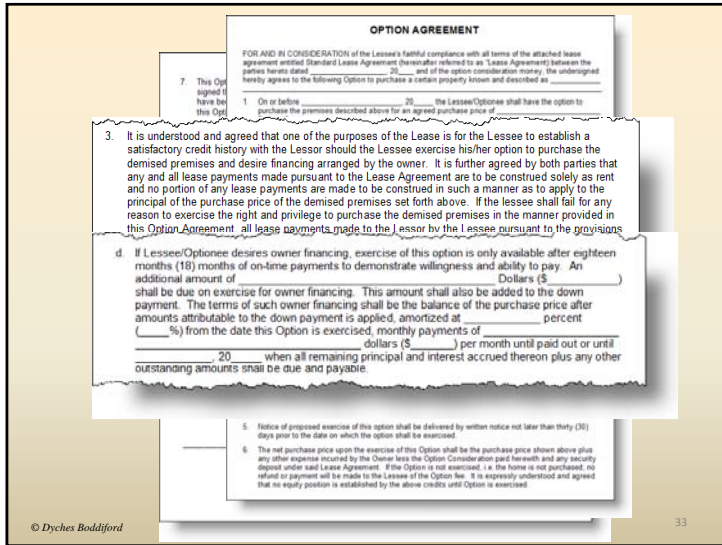
## Lease-Option

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- Same terms as Lease-Purchase.

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## Land Contract

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- Considered sale by IRS the day signed.
- Allows you to hold title until Buyer performs as agreed.
- Could agree for Buyer to pay down portion, then finance out rest with bank or investor for title to pass to Buyer.
- Has to be foreclosed in some states.

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## Pure Option

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- Advanced –
  - As a requirement for Seller financing, can negotiate getting an option to repurchase at a profit or benefit to the Buyer.
  - Secure option in land records.

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## IRA OPTION EXAMPLE

You have found a house that when fixed up will be worth at least \$150,000 as a flipper. You have been able to negotiate an all cash purchase price of \$100,000. The house needs \$5,000 in fix up for paint, carpet, etc.

You only have \$2,000 in your self-directed IRA.

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## Taking on Investors

- Personal or IRA loans
  - When selling, can get loan and wrap
  - When buying, try to get seller to subordinate
- Must be knowledgeable of the IRA rules
- Only give ownership position to investor who works in the business with you

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## Creative Financing Techniques

### What's Covered:

- Structuring Financing to Sell the Loan
- The Borrower's Credit
- Negotiating the Purchase Agreement
- Tax Treatment
- Subject-to Purchase
- Getting 0% Owner Financing
- Balloons vs. Calls

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## Creative Financing Techniques

- Wrap Around Mortgages
- Clauses for Note & Security Instrument
- Subordination Agreements
- "Walking the Mortgage" / Substitution of Collateral
- Lease-Purchase vs. Lease-Option
- Using a Land Contract
- Pure Options
- Securing an Option

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## Creative Financing Techniques

- Participating Loans
- Servicing the Loans
- Dealing with Defaults
- Modification Agreements
- Taking on Investor-Partners
- Making Money on Owner Financing  
When You are Payor

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## Real Estate Investment Using Self-Directed IRAs

- Using IRA to invest in Real Estate
- Using IRA to invest in Notes & Mortgages
- Rules for IRAs
  - Prohibited Transactions
  - Disqualified Parties
  - Unrelated Business Income Tax (UBIT)
- How to fund and build SEPs, HSAs, kid's IRAs & ESAs
- List of true self-directed Custodians with contact info

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## Profits in Partnering

- Do You Really Need a Partner
- Elements of a Deal that can be Shared
- Integrity – What it means to a R.E. Entrepreneur
- Structuring the Scenarios
- Finding Private Money Partners
- Deal Structures
- The Joint Venture

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