

Show Me The Money!!!

Real Estate Financing – Seven Sources of Funds For All the Money You Need to Buy Houses

By: Jon R. Kubas

*Real Estate Investor since 1984
Licensed Texas Real Estate Broker
Licensed Texas Mortgage Broker #3430
Past President of RICH Club from 1993-1997*

Direct Phone: (281) 397-6200
Direct Fax: (281) 440-0992
jkubas@westwindsgroup.com

*“It’s not always the cost of the money,
but the availability of money when you need it!”*

Seven Sources of Funds for Your Real Estate Deals

1. Yourself:

- Very limited
- Must have available cash or savings
- 401K
- Cash Value of Life Insurance
- Credit cards (must be disciplined)
- Personal Line of credit (If you can get one)

The Key To Your Success...Other People’s Money (OPM)

2. Seller Financing:

- Depends upon the equity in the deal
- Limited amount of Sellers can provide financing, particularly for rehab
- Usually requires funds for rehab or holding costs
- Often can take title “subject to” existing loans (Due on Sale Clause)
- Seller knows the property (collateral)
- Below Market Rates: Little or no interest on their equity
- Most sellers are not very sophisticated regarding finance and the time value of money
- No points
- No appraisal

- You structure terms: loan to value, length of loan, interest rates, payment frequency, etc.
- Substitution of Collateral Clause
- Subordination Agreement
- Seller can refinance to get cash out and let you takeover loan
- Usually no credit checks
- Very small closing costs
- Know their motivation to sell

3. Friends and family: Cash on hand, Self-Directed IRA's, Lines of credit

- May be hard to find and/or difficult to convince
- Usually have a limited amount of funds, sometimes not enough for your deal
- You will need to understand finance and be able to educate them about it
- They know you (could be good or bad!)
- No points
- You structure terms: loan to value, length of loan, interest rates, payment frequency, etc.
- Interest rates higher than seller financing and closer to Market Rates
- Tend to be flexible
- May allow Comparative Market Analysis instead of appraisal
- Usually no credit checks
- Treat them good and they'll tell their friends and family about you

4. Partners:

- Usually one provides money and the other does all the work
- Someone must have knowledge of the business
- Usually split profits 50/50 – this can be expensive money without some type of “value add”
- Partnerships are like marriages: some work and some don't
- Need solid partnership agreement delegating duties, responsibilities and procedures regarding if and when the property is liquidated

5. Hard Money or “Equity Lenders”:

- Often use their own money or lines of credit, wealthy individuals, and/or banks
- Can do “No Money Down” transactions: they will finance acquisition, rehab and closing costs
- Very familiar with and understand our business
- Virtually unlimited funds; can handle larger deals; sometimes have a minimum loan amount
- Many equity lenders available
- Each equity lender has own guidelines for their individual lending program
- Usually charge a 2 to 5 Point fee for their services
- Above Market Rates: Interest rates 10-18%, more commonly around 12-14%
- Low loan to value – generally 60-65%
- Short term – 6-12 months; could be dangerous if house doesn't sell fast
- Generally Inflexible terms; big penalties for extending loan or can't extend loan at all
- Credit often not an issue; they mostly look at property for collateral
- Closing costs are higher: Require title insurance, appraisals, processing fees, inspections, attorney to draw documents, etc. May also require taxes and insurance to be escrowed
- Great for flips – Buy, Rehab, and Sell for Cash

6. Mortgage Bankers:

- Single Source: Usually a bank or mortgage company loaning and/or servicing their own funds
- Unlimited Funds but most bankers have a limit on the total number of loans or total dollar amount of loans you can have with them at one time
- Charge a fee for their services, usually 1-2 points
- Requires cash from the borrower = Your own funds
- Can't do "No Money Down" transactions
- Credit score driven
- Market Interest Rates
- Many Variables to choose from: Loan to value: 70-90%; interest rates generally from 5.2% to 9%; fixed rate or adjustable; length of loan 15-30 years; escrow taxes and insurance
- May or may not have pre-payment penalties
- Used primarily for purchase of personal residence, second homes, refi's, loans for tenant/buyers
- Closing costs are higher: Require title insurance, appraisals, processing fees, inspections, attorney to draw documents, etc. May also require taxes and insurance to be escrowed
- Most are not familiar with our business of rehabbing
- Usually will not finance rehab properties unless you have a personal relationship with the banker
- Could have problems with length of ownership (Seasoning) if refinancing or selling

7. Mortgage Brokers:

- Unlimited Source of Funds: They locate money from banks, mortgage companies, investment funds, other institutional lenders, corporations, wealthy individuals, etc.
- Since there are many lenders, you can do more deals if you max out one
- Charge a fee for their services, usually 1-2 points
- Credit score driven
- Market Interest Rates
- Many programs available: each program varies depending on source of funds and credit score
- If one program doesn't work, can submit to other lenders and/or change programs
- Many Variables to choose from: Loan to value: 70-90%; interest rates generally from 5.2% to 9%; fixed rate or adjustable; length of loan 15-30 years; escrow taxes and insurance
- May or may not have pre-payment penalties
- Used primarily for purchase of personal residence, second homes, refi's, loans for tenant/buyers
- Closing costs are higher: Require title insurance, appraisals, processing fees, inspections, attorney to draw documents, etc. May also require taxes and insurance to be escrowed
- Most are not familiar with our business of rehabbing
- Usually will not finance rehab properties; must be in move-in condition
- Could have problems with length of ownership (Seasoning) if refinancing or selling
- Usually require cash from the borrower = Your own funds = Usually Can't do "No Money Down"

Each of these sources can provide the needed funds for your transactions. Some sources are better for particular deals than others. The key is to find the best source that will work for you in any given situation. I like to think of it like "golf clubs". You wouldn't want to go out and play against your competition with only a driver and a putter. You want every club you can get your hands on so you can make any shot in any situation. The more "clubs" (tools) you have in your bag, the more "shots" (deals) you'll be able to make! Once you become familiar with when and how to use each of these sources of funds, you'll become a *real* (estate) professional!

Jon R. Kubas and his wife Amy began buying investment property in 1984 and have been living and investing in Houston, Texas since 1990. Jon is Past-President of the Realty Investment Club of Houston (“RICH” Club from 1993-1997), and is also a licensed Texas Real Estate Broker and Texas Mortgage Broker. Jon and Amy are experts in real estate investing and finance, and have spoken many times to Real Estate Investment Associations on numerous topics, most recently teaching their home study course, **“Real Estate Wealth Systems: A Proven Cookie-Cutter System To Buying, Rehabbing, Selling, And Managing Single Family Houses”**. They buy all types of property and also provide loans to both real estate investors and homeowner-occupants. For all your real estate needs, whether you want to buy a property for yourself, want a wholesale deal, have a property you need to sell, a deal to wholesale to us, need a loan of any type, want to lend us your money, or any other item relating to real estate or real estate investing, call them in Houston at 281-397-6200, toll-free at 1-800-424-8903, or visit their website www.westwindsgroup.com.