Simultaneous Closings... Realty Vs Reality

With increased competition in the marketplace to purchase or broker existing discount real estate secured notes many note brokers in an attempt to avoid a bidding war among existing note holders to see who has the “sharpest pencil” are helping orchestrate the creation of “new” notes with property sellers with the hope of brokering the sale of this new note BEFORE it gets recorded where thereafter a universe of other note brokers can find out about it.

There are several advantageous reasons for this;

1) The note terms, conditions, & clauses can be properly set up at the outset thereby creating a much more saleable instrument. In fact standardized documentation can be utilized. Because of the ability to provide input into the note's structure the discount can be minimized.

2) A more complete and detailed inspection can take place of the collateral that will serve to secure the note. A comparable full-blown Fannie Mae type appraisal including an interior property inspection and interior color photographs is usually obtainable at this stage.

3) The prospective buyer(s) / borrower(s) can be screened more thoroughly for their employment info, income info, credit info etc.

4) The property/ note seller knows going into the transaction that he/she has a note that can be sold for instant cash liquidity rather than hoping in retrospect they did things right.

Note brokers, real estate brokers, and real estate investors who are currently using this powerful marketing approach to sell their properties faster whereby they get involved in the creation of an owner financed note have found varying degrees of success. For many there has been a whole lot of frustration. Lets explore some of the KEY ingredients I feel must be present in order to successfully put together and /or broker the simultaneous creation of a seller financed note that is to be sold.

PRESENT EQUITY

Properties that are encumbered with more than 50%-60% of their (FMV) fair market value in existing debt are not the best candidates for a simultaneous sale transaction. Most institutional note investors impose prudent limitations on the maximum exposure they feel they can safely invest funds into a deal to around the 75% –85% (LTV) loan to property value threshold. If there is more than 50%-6O% in existing debt owed against a property versus its value then there simply isn’t sufficient “meat on the bone” for us to work our magic and in most cases adequately satisfy all of the parties cash needs. This is meant to be used only as a general guideline obviously there are exceptions to every rule.

CONTROL OF THE PARTIES

These transactions have the potential dynamics of (4) four parties involved, each with distinct individual needs that must be ascertained and met.

A) THE PROPERTY SELLER- There are the sellers of the property and note who typically have unrealistic expectations over exactly what this program can do for them. They may have been told that their property could sell faster with them providing assistance in the financing. However many of them expect FULL VALUE for their note or for a funding source to fund in cash to them in excess of 85% (LTV) loan to property value even with a low down payment buyer. Some refuse to accept anything other than a FULL PURCHASE offer for their note and refuse to listen to alternative purchase programs.

Our experience has shown us that in reality a prospective property seller is NOT a good candidate for a creative simultaneous sale transaction UNLESS there is EXTREME motivation for them to move their property FAST. This motivation usually is financial and emotional in nature e.g. they have moved and purchased another home and are still responsible for debt payments on the unsold home, they have the opportunity to take advantage of a business or investment opportunity, they are going through a divorce, have health problems, or some other legal problem, etc. The fact remains that most property sellers who have substantial equity in their property do not NEED to have an ALL cash sale and realize ALL of their equity out of the property in cash at closing. This is WHY “paper” is created in the first place and, as such many of them also do not really NEED to have their entire note converted into lump sum cash as well.

B) THE REALTOR - There are the Realtors who have the property listed for sale and represent the sellers of the property. Many of them insist on creating a barrier between you and their sellers refusing to allow anyone to speak directly to them. They want to be the messenger of all news. They want the note broker to work up several creative ways to structure a sale when in fact they know little of their sellers REAL CASH NEEDS or motivation themselves.

In reality if you work with this type of realtor creative deals rarely get done. The problem in part is the inability of the realtor to sell your specific services to their sellers because they don’t understand them. Allowing the realtor to be the messenger is like having a foot doctor perform heart surgery. Insist on working with agents who will allow you to interface with their sellers so that you can extol the nuances that go along with selling their property and taking back an owner financed note. PLEASE NOTE: You are not TELLING them HOW TO put the transaction together but merely providing valuable input as to what an investor would pay for a note IF it were to be created with specific terms, etc. You certainly do not want to be perceived as making a loan here but merely acting as an advisor to the various parties involved.

Additionally many Realtors will suggest to the seller that he /she attempt to inflate the sales price of a property in an attempt to compensate for the discount to the seller for their take back note. This is not a good tactic since the contracted property sales price will need to be supported. Make sure it is clear to both the Realtor and the property seller that the contract sales price MUST be supported through an objective independent third party appraisal which will include a full interior inspection of the property.

C) THE BUYER – There are buyers for properties that come from all different backgrounds. Some of them are first time buyers, some have an impeccable credit background, and some have had prior credit blemishes. Some have strong long term job stability and employment; some are newly employed or self employed.

In reality you must understand what type of buyer you are working with or the realtor is working with. What is their employment and credit background like? Are they capable of putting down a reasonable cash down payment? What can they afford in monthly debt service on a loan? Can they afford to set aside additional funds to pay their estimated real estate property taxes and to maintain insurance on the home?

It is amazing to me how so little time is spent getting to know the prospective buyers and what their needs are. So much time is spent illustrating “theory” to the property seller’s of how they can sell their property, take back a note, and then sell the note that in many cases this type of a transaction is “sugar coated”. More time needs to be spent educating the seller and the buyer that this program is not a panacea for all situations and that there still will be certain underwriting criteria that must be followed, albeit less stringent than traditional conforming mortgage lenders. We see time after time if the right flexible terms are offered in a transaction the sales price becomes less of an issue to both the buyer and the seller.

Finding out as much as you can about the prospective buyers for a property makes a creative transaction go together much smoother. If they have had prior credit problems, then in order to minimize the seller take back note discount the note "coupon" interest rate must reflect this by being "off market" or slightly higher than a borrower who can obtain their own financing. It should be explained to these types of buyers that the seller financing offered is NOT necessarily long term permanent financing but is a way for them to get quickly into the home and then a few years from now when they have demonstrated the ability to make a timely home mortgage payment they can seek the VERY BEST rate and terms that they can qualify for at that time. If a balloon payment can be inserted into the loan terms it is best to make sure that when the balloon payment becomes due the outstanding note balance at that time of maturity does not exceed 80% of the property sales price on residential transaction.

D) THE NOTE BROKER – You provide a tremendous service to those property / note sellers who cannot sell their properties in traditional fashion to a "bank qualified" buyer / borrower. From the potential buyers /borrowers perspective you enable many home buyer's to obtain a property that they only dreamed they could afford or obtain financing for. You have spent money educating yourself and have been schooled in many alternative and creative ways to make a sale possible. You are among the minority in the marketplace offering NON CONFORMING financial solutions to real estate professionals, real estate investors, buyers, & sellers who have become myopic over the years. For this service you are entitled to earn a profit.

In reality the inexperienced note broker tends to offer a myriad of solutions to the above parties in the hopes that a transaction will come together. It is almost like offering multiple choice selections but with no right answer ever being available. They rarely have taken the time to first determine the parties REAL needs BEFORE offering solutions, and they then become frustrated when time and time again a deal never comes to fruition. By contrast many note brokers who recognize the dynamics of all of the parties potentially involved in this type of a transaction and who have properly counseled with them to determine what is most important to them can act in an advisory capacity with great ease. Those note brokers that tend to focus on HOW they can help a Realtor, real estate investor, or property seller sell their property fast, for top dollar, to a greater potential pool of buyers, or help a buyer obtain a property that they could not otherwise qualify for, and also reinforce these true "BENEFITS" rather than getting bogged down in detailed discussion on time value of money concepts are generating repeat business from satisfied customers and their referrals whom they have helped. Remember, these Seller financed type transactions aren't "off the rack" standardized loans, they can be "custom tailored" to meet each parties specific needs.
