

## **Buying Pre-Foreclosures: The Art of Buying Before the Sale**

The advantages to buying properties from homeowners in default can only be measured by the individual investor. Some do not see enough reward; some think it's too risky, while others are plagued by moral issues. Are you helping the troubled homeowner or taking advantage of his misfortune?

Both the lender and the homeowner lose in a foreclosure action. Neither wants it to happen. Both parties are motivated to resolve the situation. Motivated parties are key to the process.

The investing window of opportunity opens the day the Lis Pendens, the notice that a legal action is pending, is filed. The window closes the day the property is sold at auction. The time between these two events enables an investor to work with the homeowner and lender to create a workout strategy or a purchase of the property from the homeowner before the sale date.

The amount of time the window remains open depends solely on state and local laws, as well as the behavior of the property owner. Some states sell properties within 90-120 days from the first notice of default. In New York, the process can take a year or more.

As for the moral question, keep in mind that by dealing with a homeowner in default, you not only help him, you generally rescue the loan and maintain the value of the property (and surrounding properties) as well. If there is enough equity in the property, there is the potential to work out an arrangement that satisfies all parties and allows for a handsome profit. That's what pre-foreclosure investing is all about: buying the equity in the property, working out an arrangement with the lender and the homeowner, and then selling the property for a profit.

Investors follow these basic guidelines to ensure a successful purchase and sale:

1. Locate loans in default
2. Evaluate choices and narrow selections
3. Contact homeowner
4. Inspect property and loan documents
5. Determine homeowner's needs
6. Calculate your selling price and profits
7. Negotiate with lender, owner and lien holders
8. Close the deal, repair as necessary and sell

### **Locating Loans in Default**

The Lis Pendens is the first public notice (document) that announces a loan in default, so it makes sense to start there. Access these notices at the county courthouse, newspapers that routinely advertise these notices or through a reputable Foreclosure Service Provider.

### **Evaluate Selections & Determine Potential**

You know the default amount from the legal notices or service provider's information. Now you must estimate the property's market value. Subtract the default amount from the estimated market value to determine the gross equity in the property. This figure also reflects your gross profit potential. If there is little or no difference in the amount of debt and the market value, move on to another property. If there is a big difference, there may be enough equity in the property to make a sizeable profit.

### **Contact the Homeowner**

This is easier said than done. The homeowner is probably being bombarded with letters and calls from attorneys and bill collectors and has creditors showing up at his door. The only way to contact the homeowner is by phone, mail or in person, and chances are you will have a difficult time getting in touch with him.

Start with mailings. Indicate in your letter that you are a private investor looking for property in that part of town. Let the property owner know that you may be able to help him with his financial problems.

Demonstrating an understanding the homeowner's dilemma will help your efforts. Indicate in your letter that you may be able to stop the foreclosure, save his credit rating and provide cash for use in paying his bills and/or for relocating.

Be professional and gracious in your correspondence. Invite the homeowner to call you at his convenience. If you don't hear from him in a reasonable amount of time, say three or four weeks, follow up with another letter, perhaps worded a bit more urgently. As you get closer to the auction date you may want to send two or more letters per month.

Follow up with phone calls if you can. Be courteous, never pushy. Never interview the owner on the phone. Merely state that in order to determine whether or not you can help him, you will need to meet with him at the property. Make sure he understands that the meeting will be more productive and less time consuming if he will have the loan, mortgage and insurance documents available, as well as the foreclosure notices.

If you are going to make an offer on the property, you must have the loan, ownership, and debt or lien information. You must also assess the condition of the property and the property owner. Combined with the market value and the default amount, you have all the ingredients necessary to formulate your offer.

If you feel comfortable with it, you can visit the property in person. You may be confronted by an angry homeowner. Be polite and leave if you are asked to. Never, under any circumstance, snoop around, inspect or generally trespass unlawfully on somebody's property.

### **Meeting the Homeowner**

Use common sense and dress appropriately, something casual but not sloppy. Be sympathetic. Does the homeowner need cash? Is he waiting for a bailout? Will he go bankrupt? Find out. Review the loan and mortgage documents. Verify the loan amount, monthly payments, interest rates, taxes, etc. Review the insurance policies as well. Get all the pertinent information you can. Ask the owner if there are any other liens or judgments he may be aware of.

Inspect the property with the homeowner. Never comment on the owners' lifestyle, just the physical condition of the

property. Point out the obvious defects or items in need of major repair. Use an inspection checklist and record your information and estimated costs of repair.

Make no promises at this point. Make no offer or give the homeowner any money. Make an appointment to meet with him again if you think you want the property.

### **Preparing Your Offer**

Determine the net equity in the property. This is the difference between the market value and the default amount plus liens and repair amounts.

Negotiate with the lien holder. You may offer to satisfy the lien for 20% of the amount. Chances are the lien holder will lose everything when the property sells at auction. Buying out the lien puts more equity in the property and more money in your pocket.

Remember to include closing costs in your calculations for the purchase and sale if you intend to flip the property. Also included the carrying costs, the mortgage payments and taxes and insurances, while you hold, repair, and then resell. Also include a seller's commission if you use a broker.

Calculate every legitimate expense associated with buying, repairing, carrying and selling the property. If a large enough figure remains, you may have a very nice deal. This bottom line figure has to pay the homeowner for his property and produce a profit for you.

How much do you offer the homeowner? Some investors itemize every expense, show their calculations to the owner and offer to split the profits. Some itemize the expenses and pay the owner the remainder on the bottom line. The investor then earns his profits by the reduction in lien amounts as negotiated, savings in repairs by doing them himself, negotiating a lower seller's commission, or selling the property himself. Others still make offers based on the bottom line, and negotiate from there.