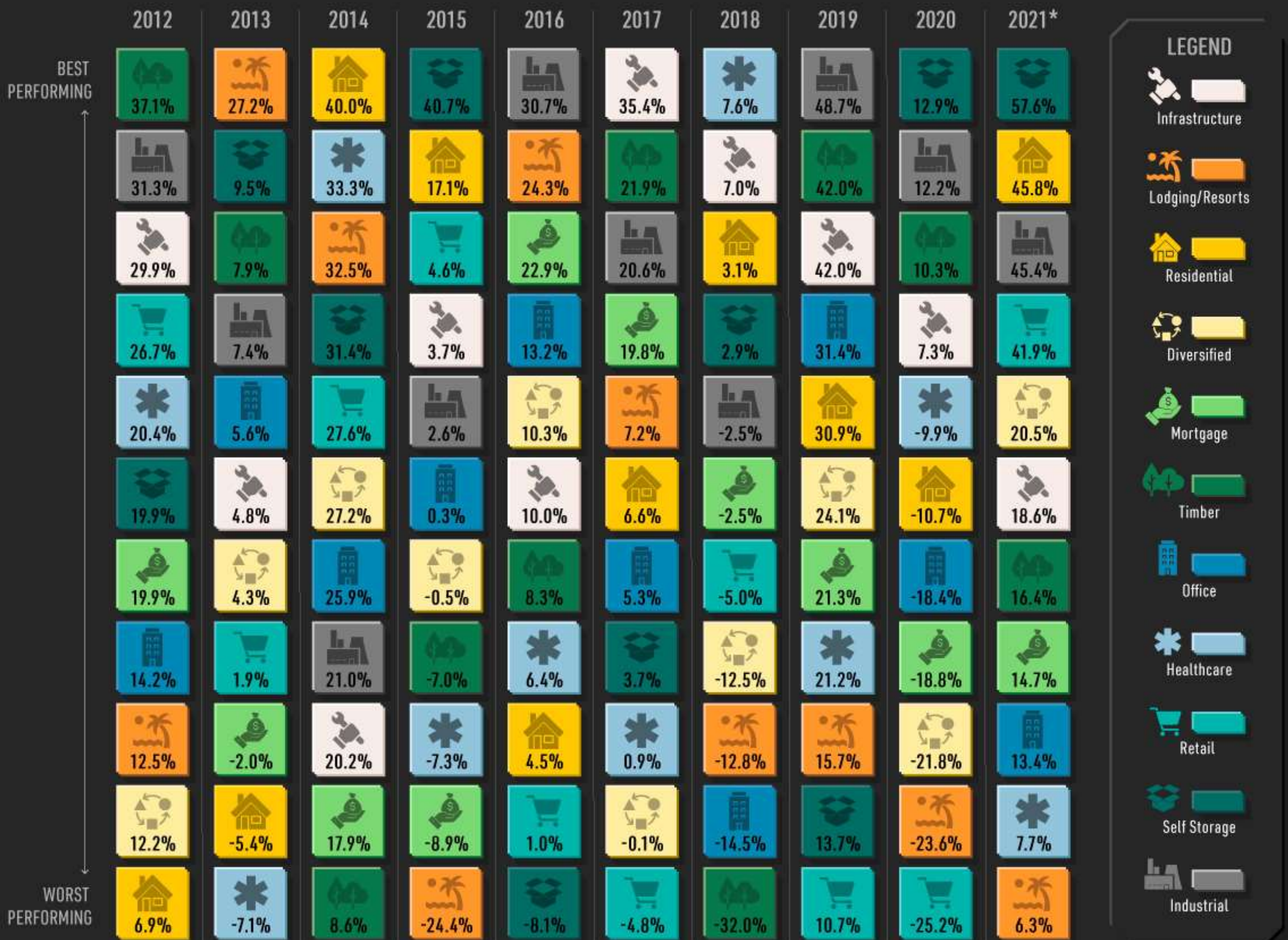
# The Paper Source

The News Of The Note Business

*January, 2022* — *Our 34th Year*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# Don't Believe Everything You Read

*by Tom Henderson*

**Here** is a little secret if you follow my articles in THE PAPER SOURCE JOURNAL, subscribe to my newsletter, hear me speak at Paper Source conventions and/or take my workshops: I will sometimes deliberately inject a wrong calculation or leave an issue unanswered just to see who is paying attention in class or who is actually reading my articles.

I am amazed at how many do not follow on their calculators. In fact, in my last two-day webinar, I had a slide that I used in one of my live seminars that had the incorrect answer. *Only one person* mentioned that he came up with a different answer. Hats off to this student who was following with his calculator and actually wanted to learn.

With this in mind, I usually mention the Rule of 72 in all my workshops. You may know that the Rule of 72 is that by dividing 72 by the interest rate you can calculate the number of years it takes to double your investment. In all the years I have been teaching, I have never had anyone challenge this axiom. Until now.

Kudos to Mary A., a student and subscriber to my newsletter. I received an email from her relaying her confusion about the Rule of 72. Mary had the audacity to test this axiom and found that her figures came nowhere near the Rule of 72. What a concept — checking your instructor's calculations! **That's good advice for all students**.

*In all the years I have been teaching, I have never had anyone challenge this. Until now.*

Let's look at a real estate note and apply the Rule of 72 to see if it holds true. For example, a $100,000 note at 10% interest paid over 20 years, with monthly payments of $965.02. Applying the Rule of 72, if we divide 72 by 10 (the interest on the note) we will conclude that it will take 7.2 years or 86.40 months (7.2 x 12 months) for this note to double the investment of $100,000. However, if we multiply 86.40 months X $965.02 payment, we come up with only $83,377.87. The investment is not even close to being doubled.

Along the same lines, by dividing $200,000 (double the investment) by 965.02 (amount of the monthly payment) tells us that it will take 207.25 months to double the $100,000 investment — not the 86.40 months as the Rule of 72 dictates.

How is the difference in the calculations explained? Could the Rule of 72 be wrong?

Without going into great depth of the advanced concepts of the time value of money, the Rule of 72 is based on the same concept as an Internal Rate of Return (IRR). By this I mean it is assumed that the monthly payments will be reinvested at the same interest rate as the note. Confusing? Not really. Relative to the note business, the Rule of 72 is the same as having a note with 0 payments with interest accruing monthly. Let's look at the note example to see if the Rule of 72 holds up to examination.

N = 86.40 months
I/YR= 10%
PV = -$100,000
PMT = 0
FV = $204,831.31

Bingo! You have doubled your money with some change to spare. Why is this? The answer is simple. The amortized note is being paid interest and principal to retire the loan. In other words, the interest is not being accrued, but rather interest is built into the payments, which includes principal and is not accrued at a 10% rate.

Contrast this to the Rule of 72, as shown above, where interest is being accrued at the same 10%. In other words, your interest is drawing interest and therefore increasing the principal. Hence, it takes a shorter time to double the initial investment.

I mentioned IRR, which is the yield for irregular payments and/or negative payments. I do go into IRRs in some of my workshops, but there is not enough time to delved in it here. Suffice it to know that IRRs also assume the payments will be

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# Note Holder Selling Signals

*by Jeff Armstrong*

Is selling an art, a science or a skill? Any salesperson (and if you are in the note business you are one) knows the answer is all three. Perhaps that is why so many people find selling is such a challenging and rewarding career.

One of the toughest parts of selling (getting the note holder to accept a discounted price) is closing – recognizing that magic moment when the note holder suddenly is ready, even eager, to sell their note to you. Unfortunately, that moment can be hard to see, even for the most seasoned note brokers and note buyers.

Here are some things to look and listen for when interacting with note holders to help you nail the sale.

**Visualizing and Ownership Language**

Listen to how the note holder describes their need for a lump sum of cash. Are they speaking about it as if they already have it? For example, they might say, "I wonder if I can get that new car I was looking at if I sell you my note."

**Follow-up, Repetition and Extras**

Is the note holder asking for more details about something you have already discussed or a clarifying point that was made (for example, "Now how does that partial option work again?")? Or are they asking if they might be able to get a little more than you offered or if you can update an option you gave them a few months ago? These are positive signs.

**Asking Permission**

When you are on the phone, do they say they have to run the numbers by another person (for example, husband, wife, accountant, lawyer). They might even seek permission from you by asking about other note holders' experiences, such as how many have sold a partial versus selling their entire note and why.

**Questions about Money and Fees**

Sometimes when a note holder muses out loud, it really means they are nearly ready to sell their note. They just want some reassurance that they are making a wise choice. For example, they might say something like, "It seems like a great deal, but it just seems like I'm

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## Tom Henderson

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reinvested at the same rate as the loan, like the Rule of 72.

Does this mean the Rule of 72 and IRR are useless in evaluating notes? Heavens, no. Although amortized loans or notes are calculated differently than the Rule of 72 and IRR, they both are a good first step to analyze a note.

From this article there are three major points to remember:

1. The Rule of 72 is not calculated the same as an amortized note.

2. In my workshops and articles, I sometimes present an erroneous answer to determine who is following and who is not. (SECRET: I sometimes make mistakes, also!!!)

3. You should be checking all work from all instructors, including me.

By following the exercises or issues with your calculator, you will learn quicker and understand better.

Homework: Did I make any mistakes in this article? What? You did not check?

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*He has been called "the best kept secret" of instructors in the nation. His* Note Professor Notebook *is available at his website* hpNOTES.com. *Contact Tom if you need help with structuring or selling your notes.*

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### Should You Start With Non-Performing?

*Why do so many people want to buy a non-performing note for their first note purchase? Does everyone think they are going to make one call to the payor and get them paying again and make a fortune? — Kenneth Spink*

The process is fairly simple and a lot of remedies are afforded to secured creditors. There is clearly more money in non-performing rather than being farther along the food chain and buying performing but also more risk; Manageable, predictable, and measurable risk...being a niche, nuanced and specialized investment, the yields and returns should reflect that reality. — Matt Kelley

Mainly because they took some weekend warrior training program that they dropped way too much money on. — Christopher Seveney

Low cost of entry is appealing, being able to gamble on sweat equity also lowers that cost of entry, but yes, it could end up in a forever taking and expensive foreclosure process, but there are all these professionals telling people it can be done for "not that much money" in the hopes of securing some new clients.
— Jeremy Finn

Many people are more comfortable putting in sweat equity for the possibility of a higher return rather than a higher capital investment. — Jenni Rudder

My first note purchases were 4 non-performing contracts for deed. That was in Sept., 2021. Since then I have resolved all 4 in different ways on each. Difference is, I have a mentor and mastermind community who helped me learn how to do this. — Steven Tucker

My first note purchase was a “boring” performer at a 7% face rate. I paid par. Although I have and continue to invest in education, I also like to learn while I earn. Buying a boring note exposed me to the process of buying paper. I continue to collect on that note today. So boring. — Marco Bario

My first note(s) were npn in 2012. Bought as a pair for $5,500. But today those prices don't happen. My 3rd note was $12,500. We took the asset back after foreclosure and then rented it for 8 months. After that we sold the property for $68k. — Dave Putz

### Contracts For Deed vs. Mortgages

*Other than the exit (foreclosure time and expense) why else would one choose (or not choose) contracts for deed (CFD's) above mortgages? — Ricky Lee*

Why to *not* choose: CFD’s for investors are considered extreme risk. The debtors are usually under-qualified and the properties low value while in areas that are prohibitively expensive (relative to the property value and investment) to collect upon in the probable event of default.

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## Jeff Armstrong

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losing money.” Remind them of the reasons for the discount – that what they have is just a promise to pay and not a guarantee- how selling their note will save them time, money and stress in the long run and that a lump sum of cash in hand is better than those small monthly payments. What you are doing is easing their mind that they won’t have any reason to regret selling their note.

These are just a few of the ways to recognize when the note holder might be ready to sell. Practice listening for these and other signals note holders divulge while you are communicating with them and you will soon see your acceptance rates go up. Be kind, keep safe and stay healthy. Remember success demands action, keep on marketing, it’s going to work! TWITA! (That’s What I’m Talkin’ About!)

*Jeff Armstrong of Armstrong Capital has been a note investor and broker specializing in the performing seller financed note industry since 1991. For more information on how he can help you with your note business, note investments, note appraisals or to request pricing options on a note visit* armstrongcapital.com *to email him and subscribe to Jeff’s Weekly Training & Tips Newsletter.*

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CFD or seller carry back is somewhat common in the Midwest and rural areas due to strict lending criteria on lower value homes. This allows for a sale which would otherwise be impossible. — Matt Kelley

## Split Payments

*Does anyone actually sell split payments? — David Rosenhaus*

Split payment is a type of partial where the monthly payment is split between two parties. I have not done this as there is a possibility of running afoul of securities laws. I sell and buy partials where full monthly payments goes to one party until their period if receiving payments end. — Sri Gan

When you are splitting each monthly payment there are questions concerning security laws that attorneys have brought up to me that can be a security violation. In my opinion, you should never use the word split payment; it drives security attorneys nuts.

In my opinion, (I am not an attorney and not giving legal advice) a safer way to go is with a partial than a split payment. In a partial the entire monthly payment goes to the partial buyer for the agreed-upon number of payments that are made, then reverts back to the original note seller. You are treating the note as an asset. You assign the note and mortgage/deed of trust to the partial buyer during the number of payments agreed upon, then the note and mortgage/deed of trust is assigned back to you as the initial seller.

You can also borrow against the note (hypothecation) using the performing note as collateral for the loan. In hypothecation, you can have it set up with the servicer that with each monthly payment, the lender receives his payment and you as the borrower receive the balance. The payment is split up because you owe the lender a monthly payment. This is perfectly legal. We do both hypothecation and partials. Just saying that "the payment is split" does not give us enough information to determine why it is split, which makes a big difference as far as security laws are concerned. — Jay Redding

## Notes And 1031 Exchanges

*Can one sell a property and 1031 into a note? — Ricky Lee*

No. A 1031 exchange (a.k.a. Starker exchange, tax-deferred exchange, or like-kind exchange) is a real estate transaction involving properties used for investment or in a trade or business. The proceeds from the relinquished property must be used for the purchase of a replacement property. Notes do not qualify as property under Section 1031 of the Internal Revenue Code, which states that certain types of property are specifically excluded from Section 1031 treatment:

- Inventory or stock in trade
- Stocks, bonds, or notes
- Other securities or debt
- Partnership interests
- Certificates of trust

— Bill Mencarow

Open up a SDIRA (self-directed IRA) and purchase notes with it. All proceeds can be tax-deferred. — Artie Aseg

## Why Notes?

*What got you into buying mortgage notes? — Antonio Arizmendi*

Bought a trailer park on a note. Fixed it up and sold it (four times) but the bank loans never got approved so I carried the paper and BAM! — Bob Zachmeier

Cash flow, no property to manage or in my name as a liability or for creditors to garnish. — Juan Zapata

I was looking for a new way to invest. Tired of the headaches of being a landlord, I came across Paige Panzarello (cashflowchick.com).and started getting educated. I get no compensation for telling you about her, but she's great! Notes are not for everyone, but they are for me!— Michelle Tenebruso Gradis

Cashflow. Asset-backed investments. Flexibility. Solid returns. — Tyson Eimers

Initially it was a way to sell properties that needed work and I had no operating budget to fix them up. We sold properties on terms for the same price as market rent. From there I wanted to buy more properties and recognized this as a less expensive way to acquire properties. — Nathan Turner

I give my tenants all the credit for getting me into notes. Landlords know what I mean. — Bill Mencarow

# Self-Liquidating Loans

A true self-liquidating loan (or self-liquidating offer) is a form of short- or intermediate-term credit instrument made against the liquidation of inventory or the sale of goods. It is repaid with money generated by the assets it is used to purchase. The repayment schedule and maturity of a self-liquidating loan are timed to coincide with when the assets are expected to produce income. These loans are intended to finance purchases that will quickly and reliably generate cash.

Although few loans are legally named "self-liquidating," the term is commonly used by bankers to refer to lending arrangements that work in this manner. It is also used by some scam artists, as will be explained.

The typical self-liquidating loan is one made to farmers against the sale of crops. The revenue from the sale is used to repay the loan. A retail business might use a self-liquidating loan to purchase extra inventory in anticipation of the holiday shopping season. The revenue generated from selling that inventory would then be used to repay the loan.

*Self-liquidating loans don't make sense for buying fixed or depreciable assets.*

Self-liquidating loans are not always a wise credit choice for businesses. For example, they do not make sense for buying fixed assets, such as real estate, or depreciable assets, such as machinery or office equipment.

In many ways, a self-liquidating loan is much like a revenue bond with a sinking-fund feature. Revenue bonds are secured by specific revenue sources, such as tolls in the case of a highway, and a sinking fund dedicates money to be set aside for debt settlement.

**Beware Of The Scam**

This is not what fraudsters mean when they speak of millions to be made using self-liquidating loans and when they speak of borrowing thousands of dollars that never have to be paid back. Some who make money on these "opportunities" are those who charge for a "special report." All the others make money from up-front fees of one kind or another or by getting you to give them your bank account number or hand over your securities for "investment."

First you are told that you can borrow thousands of dollars with no collateral and no credit. The bank doesn't even have to know you. Then you are told that once the bank hands over the money you use some of it to purchase “Letters of Credit” or “debentures” that you turn over to the bank as collateral for the loan. (First the bank gives you the money, *then* they get their collateral. If banks did that, they'd all go broke in a week!)

According to the scam, you don't really get the full loan, only a portion. The rest is turned over to (the terms vary) “special investment bankers” or a “trader” or a “dealer” or a “commitment holder” or a “grand master” who invests it into a “high-yield investment program” using “arbitrage.” The proceeds from the investment supposedly pay off the loan, give you the balance of the amount you borrowed plus some more, and you walk off a millionaire. And this is all accomplished within a few days or even overnight!

Regardless of how badly you or your company may need money, this loan scenario simply isn't logical, and of one thing you may be absolutely certain — banking is as logical a business as it gets. It’s a SCAM!

(Portions of this article appear at investopedia.com)

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# January 31 Deadline For Filing 1098s

*by Roger J. McClure, J.D.*

**Do** you know whether or not you must file a Form 1098 with the IRS and provide one to your borrowers? There are general rules to follow:

1) If you or your company, corporation, partnership or trust are in a trade or business and you receive mortgage interest incident to your trade or business, and you or the entity receive interest payments from individuals and any individual paid you more than $600 in interest in a calendar year, you must provide a Form 1098 by January 31 of each year to each individual who paid you at least $600 of mortgage interest in the last year. You list on the 1098 all of the interest received and send a copy to the IRS. You must also file Form 1098 and 1096 with the IRS by Feb. 28.

2) If you or your entity meet the qualifications under #1, you do not have to report to the IRS or the payor any interest paid by a corporation, trust, company, estate or other entity which is not an individual.

3) If you meet the qualifications under #1, you only report individuals whose mortgage interest payments generate more than $600 per mortgage in one calendar year.

4) If you or your entity are not in a trade or business or your receipt of mortgage interest is not incident to a trade or business, then you do not have to send in Form 1098 to the IRS or your borrowers.

**Example 1.** You buy, hold and sell mortgages from time to time. You usually only have about three or four mortgages during the year which you hold in your name. You report your interest income on Schedule B and your interest and other expenses on Schedule A. This amount of activity does not rise to a trade or business but is an investment activity.

**Example 2.** You formed a corporation, licensed it as a mortgage lender, and set up an office in your home. Your spouse works and the lending corporation is your main source of income. You make about 100 loans a year and borrow a large part of your capital. This constitutes being in a trade or business and you must provide 1098s to your qualifying non-corporate borrowers and to the IRS.

**Example 3.** The same facts as Example 2, but five of the mortgages you hold each paid less than $600 in mortgage interest. You report none of the payors who paid less than $600 of mortgage interest in the last calendar year.

**Example 4.** Your corporation's pension fund buys and holds to maturity about 10 mortgages and continues to buy more as the pension fund grows. The pension fund is a passive investor, not intending to be in a trade or business. The pension fund provides no 1098s to anyone.

**Example 5.** You have a small loan company which you conduct as a side business from your regular job. It is not incorporated and you report its income and expenses on a Schedule C. You buy, sell or hold about 10 to 15 mortgages a year. You want to be viewed by the IRS as in a trade or business so that you can deduct the expenses of conducting your loan business on a Schedule C. Because you want to be treated for all purposes as conducting a trade or business, you provide 1098s to your qualifying non-corporate borrowers and the IRS.

The critical elements in mortgage interest reporting are that you or your entity must be engaged in a trade or business and your receipt of mortgage interest is incident to that trade or business. You or your entity do not have to be in the trade or business of mortgage lending. The loan servicer who has sufficient information to report mortgage interest subject to the Section 6050H reporting requirement must report it.

If you do not make the required 1098 reports, you can be subject to a fine of $50 per form up to $100,000. In general, if you cannot determine whether you are or are not receiving mortgage interest incident to a trade or business, it is best to file the reports to avoid the penalties and to add further support to your claim for the deduction of your lending business expenses.

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# The SAFE Act, Dodd-Frank & Seller Carrybacks

**Part I**

*by J. Robert Eckley, J.D.*

There are three sources for alternative real estate finance: Seller-carries; a private secondary market for owner-carry paper resale; and private, non-conventional lenders.

In some cases, the owner-carry is PRIMARY, meaning directly between seller and buyer; in others it can be "SECOND PARTY" such as owner selling to an investor who then leases (many times with option) or sells back to the buyer on an "owner-carry" or "THIRD PARTY" where the investor simply puts up the money to make a seller-buyer deal work in the same way a bank might or even "FOURTH PARTY" as when the paper generated in FIRST OR SECOND PARTY deals is then sold to a paper-buyer.

In some cases it can be as simple as owner selling to buyer as a financier who then agrees to lease back from buyer, sometimes with an option to purchase at some point.

There are four approach tools and disposal methods for this, and these represent nothing more than a return to what worked in the late '80s. Here are the "old/new" tools:
(1) lease/purchase; (2) lease/option; [note: (1) and (2) are NOT THE SAME THING] (3) all inclusive deed of trust; (4) all inclusive mortgage; (5) installment land agreement or land sale contract.

*The law actually tries to prohibit all private real estate transactions and make bank financing mandatory.*

Incidentally, seller-carries are exempt from RESPA! RESPA (the Real Estate Settlement Procedures Act) excludes "an all cash sale, a sale where the individual home seller takes back the mortgage (seller-carry), a rental property transaction or other business purpose transaction."

There are two newer federal laws that affect seller financing. On July 30, 2008, President Bush signed into law the Secure and Fair Enforcement for Mortgage Licensing Act (the "SAFE" Act). The SAFE Act requires licensing or registration of loan originators. On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act or "DFA"). The Dodd-Frank Act ("DFA") restructures the oversight of financial regulation and allocates the consumer portion of it to a new agency called the Consumer Financial Protection Bureau ("CFPB"). The DFA also includes amendments to the Truth in Lending Act ("TILA") and RESPA. Both of these laws affect seller financing, except to the extent exempted.

## THE CFPB RULES FOR SELLER-CARRIES

**What is a "Loan Originator?"**

The Consumer Financial Protection Bureau (CFPB) released the original rule on January 20, 2013, as part of its implementation of amendments to the Truth in Lending Act (TILA) made by the DFA on July 21, 2010. The rule took effect on January 10, 2014, except for two important provisions related to loan originator qualifications that took effect on June 1, 2013. See 12 CFR section 1026.36.

Yes, it is true, the two acts are actually trying to tell private citizens what they can do with their own property and what transactions they can do with their own money without having also to pay the banks a percentage of the entire deal to handle it for them. It actually tries to prohibit all private transactions and make bank intervention mandatory. But, as in all law, after the shock subsides of seeing the Feds with their noses so deeply in the private financing and loan affairs of the average citizen and after some good lawyers look at this, there are places where the Acts miss the mark entirely – and apparently unintentionally – and still permit private transactions.

The new rules provide in general that only licensed "Loan Originators" (usually called a licensed mortgage originator or "LMO") can approve the borrower's credit or approve certain tough buyer terms in most consumer residential seller-carry transactions; otherwise the transaction itself is void, and those who facilitated it without being an LMO are in violation (there are civil and criminal penalties).

The new Final Rule establishing "Loan Originator Compensation Requirements" not only covers the new "loan originator" definitions, but also sets allowable fees. The rule applies broadly to loan originators, including seller-financers that do not qualify for an exclusion from the definition of "loan originator." One who falls into the definition of a "loan originator" must then comply with strict licensure requirements and underwriting duties.

After making the general statements, above, there are some exceptions and qualifications.

**A Broad Definition**

The definition of a "loan originator" is now very broad. It covers anyone who, for compensation, performs any activities related to the origination of mortgage loans, including (but not limited to): taking an application or offering, arranging, or assisting a consumer in obtaining or applying for credit.

TILA, as amended, and CFPB's implementing regulations exclude from the definition of loan originator some sellers who provide seller financing, but only if they meet narrowly-defined exclusions (below). Because the requirements are extremely complex, unless seller financers qualify for exclusion, they will as a practical matter have to use

*Seller-carries are exempt from RESPA.*

another approach for financing the sale of the property, including engaging a licensed loan originator ("LMO") without risking penalties for performing loan origination activities themselves. This is similar to the situation under the SAFE Act's loan originator licensing requirements where, unless one is exempt from licensing under the state law enacted to implement the SAFE Act, it is not usually practicable to provide seller financing directly.

**Two Seller-Carry Exclusion Categories**

In response to many commentators, CFPB provided some flexibility in the new Final Rule by excluding from the definition of "loan originator" two categories of seller financing:

(1) those sellers who sell 3 or fewer properties in any 12-month period

(2) those sellers who sell only one in any 12-month period, and in both cases meet other criteria.

If a seller sells one property using the less restrictive exclusion rules then one is unable to sell another within 12 months of the first sale, as the first sale would not qualify for the more astringent standards of the "more-than-one-sale-every 12 months" exclusion. Thus, if the seller sells under exclusion 1, above, the single-sale exclusion, then seeks to sell a second property, the safest course would be to wait for the expiration of 12 months after consummation of the first sale before selling the second property.

The only other option for the seller if there was any doubt which exclusion to use would be to routinely qualify under the 3-sale exclusion, since in that case the second sale and even third sale is always permissible inside the 12 months.

Though the CFPB made minor changes to the statute, such as the one property exclusion noted above and not requiring proof of documentation of a borrower's ability to repay, the Bureau determined to not eliminate the criteria in the seller financing exclusion as defined in the Dodd-Frank Act. Accordingly, credit verifications and ability-to-pay evaluations should continue to be made.

**Continued next month**

*J. Robert Eckley is an attorney, former Realtor® and builder, present Realtor® Affiliate, litigator, forensic engineer and educator who deals primarily in real estate, banking, construction and finance on a multi-state basis.*

*He is president of the law firm of ECKLEY & ASSOCIATES, a multi-state practice, is the Forensic Manager of National BuildMasters, a forensic contractor, and is President of and equity-holder in The Westcourt Financial Group, Inc., an investment firm and corporate owner of the Institute of Real Estate Law & Standards. His present practice focuses upon real estate and financing, banking prosecution and defense, agency prosecution and defense, securities, investment and foreclosure litigation.*
*Phone: 800-999-4LAW*

# Creating Notes By Flipping

*by Del Ashby*

We will look back upon right now as one of the best times for note brokers and investors in decades. Mortgagors (payors) are faced with buying gas and food or paying the mortgage. Note holders are panicked.

Faced with non-payment, most private note holders don't know what to do. They just want to be rid of the problem. Usually they don't know where to turn, and they definitely don't want the property back. After all, they had to take back paper to sell it in the first place! That is, of course, where we come in.

Here's a transaction I did and how you might want to try the same.

### The Problem

I have chosen a couple of areas of the country where I have developed a few contacts and some knowledge of the local area. One of those is in New Mexico. I ran an ad in the local newspaper wanting to buy real estate contracts or mortgages. From that ad, I got five calls.

One of the calls was from a lady, let's call her Judy, with a problem like I described above. She had a real estate contract (in New Mexico, seller carryback notes are "contracts") that had fallen 5 months behind, and the "owner/tenant" refused to leave. To her credit, Judy had done a lot of the right stuff to recover the property but wasn't succeeding. After a few questions, I decided to meet with her at the local title company's offices.

*Faced with non-payment, most private note holders don't know what to do. They just want to be rid of the problem. That's where we come in.*

After the first meeting, I had a good insight to what she would accept and how to approach the opportunity. I took the documents with me to study. The note was seasoned for 8 years, had a face interest rate of 8%, and was on a 3BR/2 bath, 1560 square foot house. The outstanding balance was about $37,500. The occupant of the house was on disability and had been making $400 monthly payments. She had failed to make the tax and insurance payments for the last two years. Judy, the contract holder, had to pay them to protect her interests. Judy was also retired with not a lot of income so she had reached the end of her rope.

### The Offer

I offered Judy $32,000, and she agreed to sell the contract to me. I also told her that she would be responsible for getting the property vacated before we could go to settlement. I guided her to the right attorney to handle that issue. The occupant immediately turned to legal aid, so I knew it was going to take awhile.

**Knowing the contract was in default, I put a special clause in my purchase agreement that if the default was not cured and Judy foreclosed, I would have the right to buy the house from her for the same price I had offered for the real estate contract.**

### Two Options

I told Judy that I was leaving and that I would return when she had the house vacant and we could then go to closing. I left myself the option to extend the contract at will. I then left with the understanding that she would call me if I could help her further or if she succeeded in getting the house vacated.

I kept in touch with her, and eventually she was able to foreclose and get title to the house. It was now empty, and she was ready to sell it to me at our agreed-upon price of $32,000. I immediately headed back to New Mexico.

After inspecting the house I concluded that I had two options. First, I could keep it, rehab it and sell it for around $95,000. Second, I could try to sell it as-is to an investor I knew in that town. Since I don't live in New Mexico and couldn't supervise a rehab, I chose the latter option.

### The Investor

Within 24 hours after I was back in town I had the house keys and called the investor. I simply told him I had a house he needed to see.
I offered to pick him up the next morning.

We walked through the house, out to the back yard, and I saw him start to write on a small pad he had brought with him. He handed me the sheet of paper on which he had written: $45,000, 8%, 10 years, $5,000 down.

We walked on and neither of us said anything. I finally said, “I really would like to do business with you, but I can’t do it at that price. The very best I could do would be $53,000.” No more discussion. I took him back home.

I returned to the house, was unlocking the door, and my cell phone rang. It was his real estate agent/advisor. She immediately told me he wanted the deal as I had offered it. I said okay, and it was effectively sold.

### Bought & Sold In 4 1/2 Hours

Five days later, at 10:00 a.m., I closed on the purchase of the house from Judy. I paid $32,000 cash plus $150.00 in closing costs. At 2:30 that afternoon I sold the house to the investor for $53,000 with $5,000 cash to me and a real estate contract payable to me in the amount of $48,000 at 8% for 10 years. The buyer paid all closing costs. Not a bad day’s work.

### The Key Steps

Here are the key steps I used, and you could do the same.

First, as you know, there are different kinds of debt instruments. I do not care for trust deeds. I prefer real estate contracts. Mortgages are my second choice. This has mostly to do with how each of these instruments handle defaults.

*This is one of the best times for note investors and brokers in decades!*

**Step one** is to choose a jurisdiction or two that uses your chosen kind of debt instrument.

**Step two** is to travel to that area to get to know a little about the good and bad sections of the town. While there you will also want to meet the manager of a title company and get the names of a couple of the smaller, well-respected real estate brokers in town. They will also know all the other professionals in town that you may need. Screen their recommendations yourself for your own comfort level.

**Step three** is to find out the main newspaper in town and run an ad. I ran it for a month and it said simply: **Want to buy real estate contracts. I can pay cash. Call Del at 1-800-477-xxxx.**

An alternative to paying for a newspaper ad is to post on craigslist.com for free. The drawback is that you will have to re-post every few days to keep your ad near the top of the listings.

**Step four** is to return calls and listen carefully for them to disclose their problem as well as all the other primary pertinent information you will need. Get the address of the property so you can determine if it is even in a neighborhood with which you are comfortable.

### Determining The Value

You are now prepared to drive by the property or have someone else look it over from the street. You then want to head for your chosen real estate broker and ask them to run **recent sold** comps for you. That will give you a price per square foot for other houses in the area. They should be able to give you those figures for properties both in fix-up condition and for nice, ready to sell condition.

**DO NOT depend on tax appraisals or assessments!**

You can now apply those figures to your prospective property to get a good insight for values and what you can afford to do.

When you have reached this point, simply use your normal buying approach, being careful to understand their problem. **You don’t want to buy into their problem unless you can and want to solve the problem profitably.**

Especially if you plan to resell rather than hold the property, keep your mouth shut about your prices, strategies and the like. The title company can’t ethically or legally disclose details of your transaction to the other party. Notwithstanding, I still meet the closing agent in advance and tell them that such disclosure is not to be made or discussed in the presence of other parties.

Now is a great time to help other people solve their problems — and make a handsome return in the process.

*Del Ashby has been buying notes for decades. He wrote* Make Money Trading Mortgages, *which every note broker and investor should read and re-read often. It is available at* store.PaperSourceOnline.com

# 23 Tips For Note Investors & Brokers

*by W. J. Mencarow*

1. Never ask an investor for a quote unless you are in direct contact with the note holder.

2. Never believe a website that claims to be a note investment company unless you know independently that they are for real. 95%+ are brokers.

3. Never buy financial training from an infomercial.

4. Never use private investors unless you have brokered A LOT of notes with institutional investors and have learned all the pitfalls.

5. Get to know who the genuine institutional investors are — there are very few, and most of them are in THE PAPER SOURCE REGISTRY OF NOTE INVESTORS.

6. Don't buy training by companies that sell notes. No one can ethically teach you how to get a great deal on a note and then try to sell you one.

7. You won't make any money as a note "finder." You have to be a genuine broker who does the due diligence investors expect.

8. As a note broker, make it your goal to know at least as much about the note business as your investor.

9. Gather as much information as possible about the note, property and payor *before* you contact an investor.

10. Develop trust with the note holder by being a person who inspires trust.

*"Opportunity is missed by most people because it is dressed in overalls and looks like work." — Thomas Edison*

11. Verify everything you can about the note, property and payor, including what the note holder tells you, before you commit to the purchase or contact an investor.

12. Tell the investor everything you know about the deal, the good and the bad — hold nothing back — and as you learn more, tell the investor.

13. The bigger the deal the less likely it is to close — make it big on little deals (John Schaub's rule; www.johnschaub.com).

14. Make it your goal that for every X number of notes you broker that you will keep one for yourself (Mike Meeker's rule).

15. Sell investors partials and keep the back ends for yourself (and keep track of who owns the front ends!).

16. Devote at least 80% of your time and resources to marketing for notes. Jeff Armstrong has some great marketing training: armstrongcapital.com.

17. Never let a note holder go uncontacted for more than a month. Keep a tickler file and get in touch with those who have turned you down. People's circumstances are always changing; the person who said "no" last time might say "yes" today.

18. Nobody knows as much as you think they do. Don't put blind faith in any teacher.

19. Keep learning — what worked last year may not work today.

20. The reason most people fail in the note business is because they give up too soon. Knocked down? Get up!

21. Good judgment comes from experience, and experience comes from bad judgment.

22. Treat every setback as a success, because its a learning opportunity. When Thomas Edison had tried thousands of materials for his light bulb filament and none of them worked, someone said how discouraged he must be at his failures. *"I have not failed,"* said Edison. *"I've just found 10,000 ways that won't work!"*

He also once said, *"Opportunity is missed by most people because it is dressed in overalls and looks like work."*

23. This is NOT a money business. It is a people business. You're in the business of solving peoples' problems. Believe and project that sincerely and you'll likely succeed.

## The $50 Lesson

I recently asked my neighbors' little girl what she wanted to be when she grows up. She said she wanted to be president of the United States some day.

Her parents, both politically liberal, were standing there, so I asked her, "If you were president what would be the first thing you would do?"

She replied, "I'd give food and houses to all the homeless people."

Her parents beamed with pride.

"Wow, what a worthy goal!" I told her, "But you don't have to wait until you're president to do that.

"You can come over to my house and mow the lawn, pull weeds and rake my yard, and I'll pay you $50.00.

"Then I'll take you over to the grocery store where the homeless guy hangs out, and you can give him the $50.00 to use toward food and a new house."

She thought that over for a few seconds, then she looked me straight in the eye and asked,

"Why doesn't the homeless guy come over and do the work, and you can just pay him the $50.00?"

Her parents still aren't speaking to me.