

**THE ALL-NEW
REAL ESTATE
FORECLOSURE
SHORT-SELLING
UNDERWATER
PROPERTY AUCTION
POSITIVE
CASH FLOW BOOK**

*Your Ultimate Guide to Making Money
in a Crashing Market*

Chantal Howell Carey & Bill Carey

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PREFACE

Welcome to the greatest real estate money-making opportunity of our lifetime. The real estate market has crashed. For the bold and savvy real estate investor, *now* is the time to buy. Buy as much real estate as you can as quickly as you can and consider financing the sale as the banker for quick cash and cash flow or holding the property for cash flow and future cash profit. You will become a multi-millionaire if you do.

The United States government is proposing to pump \$9.7 trillion into the economy over the next four years according to the *New York Post* (February 10, 2009). One trillion dollars will be in the form of an economic stimulus. Three trillion dollars will be in the form of lending and spending programs. Another \$5.7 trillion will be in the form of agreements to provide loan guarantees or aid to various entities at home and abroad.

How many trillions will go directly into the real estate and mortgage markets has yet to be seen. The indirect impact of all this government spending on the real estate market is huge. Real estate prices will be going back up. Inflation, not deflation, is in the pipeline.

Strategy

You must have a strategy in order to make money investing in a crashing real estate market. Some investors use a quick cash strategy to buy and flip properties immediately. Some investors use a long-term wealth building strategy to generate cash flow and hold properties for future appreciation. We recommend you use both strategies. We will show you the pros and cons of each.

Foreclosures

Twelve million foreclosures are predicted to occur in the next four years. In Part One of *The All-New Real Estate Foreclosure, Short-Selling, Underwater, Property Auction, Positive Cash Flow Book* we present the all-new investment tactics needed to take advantage of this foreclosure bonanza. These new tactics include coupling short-selling and auctioning with the government bailout of the residential real estate mortgage and housing industry.

We will show you why it is in your best interest to stop buying foreclosures at the white elephant sales (the courthouse steps). We will take you inside lender loss mitigation departments and show you the 12 factors that a lender will consider before accepting your short-sale offer. We will also show you how to buy the mortgage in foreclosure from the lender at a short-sale discount.

Sellers Are the New Bankers

In Part Two we present what you must do over the next four years to become a multimillionaire investing in real estate. This starts with understanding that in a crashing real estate market, sellers are the new bankers for real estate investors.

The passage of new U.S. federal lending laws restricts easy access to new mortgage financing for all real estate buyers, especially investors. Lenders will want to verify everything about a potential borrower including job stability, monthly income and expenses, credit history, financial strength, and ability to make mortgage payments.

If you have a down payment and you have to obtain a new loan from a bank for the balance of the purchase price, unless you have perfect credit, you will not get financing. Investor buyers will have to have cash or look to the seller as banker in order to finance their real estate deals.

Success Buying or Selling

Your real estate investing success in a crashing real estate market will be determined by two factors. Buying successfully is the first factor. We

call this Win Going In. Selling successfully is the second factor. We call this No Doubt Getting Out.

Win Going In

Again, without perfect credit, the only loans available to investors will be offered by sellers. We will show you how to negotiate with the seller so that the seller will jump at the opportunity to be the banker and sell you his property. You will Win Going In because you have negotiated the right price *and* the right terms. By buying for the right price and the right terms, you can make money when you sell.

No Doubt Getting Out

You will have No Doubt Getting Out because when you sell, you will sell for the right terms *and* the right price. By employing seller as banker financing when you sell you will generate cash and positive cash flow carrying the mortgage for your buyers.

Auctioning Your Property for Top Dollar

We show you how to auction your property for top dollar. By using an auction you will receive the highest price possible in a crashing market. We are not talking about a foreclosure auction where the opening bid starts low and you hope buyers bid up the price. We are talking about a version of a Dutch auction where the opening bid starts high and whoever makes the first bid below the opening bid gets the property.

A New Technique

We present a new technique that successful real estate investors can add to their repertoire to make money investing in a crashing market. This technique is Buy Low and Sell Lower. Using our experience buying and selling we answer two important questions. How does this technique work? How do you make money using this technique?

Cash and Cash Flow Is King

In normal real estate markets cash is king. This means that if you can pay cash for real estate you typically can get a lower price and therefore a better buy.

Example

Let's look at an example. A seller is asking \$1,000,000 for his New York City condo. In a normal real estate market you, as the buyer, would be concerned with how are you going to come up with the \$1,000,000 asking price. If you had \$900,000 to \$950,000 in cash, you could negotiate a good price with the seller. In a crashing market, the seller may accept \$900,000 or less if you have cash.

Cash Price Savings

Asking price	\$1,000,000
Cash price	– \$ 900,000
Cash price savings	\$ 100,000

In a crashing real estate market cash and cash flow is king. You must create cash and positive cash flow on every one of your deals. Otherwise you will go broke. We show you how to make a profit, create a positive cash flow, and stay in the game as a successful real estate investor.

The All-New Real Estate Foreclosure, Short-Selling, Underwater, Property Auction, Positive Cash Flow Book is the only book that shows you how to start with little or no knowledge about investing in real estate and jump in and make money in a crashing market. While everyone else is standing on the sidelines afraid to act, you will be winning the real estate investing game.

When we developed and produced the Foreclosure Training for Robert Allen, our students in Baltimore and Los Angeles were able to put into practice our insider knowledge and make money investing in foreclosures immediately. With *The All-New Real Estate Foreclosure, Short-Selling, Underwater, Property Auction, Positive Cash Flow Book*, you will be able to do what our students did coast to coast and beyond.

I N T R O D U C T I O N

Over the years, we have traveled throughout the world teaching various financial, real estate, success, and trust educational programs through Howell Carey International University (HCIU). We are always striving to be on the leading edge for ourselves and our students. Our investor, brokerage, trustee, and educators experience in the real estate industry lets us give you the practical knowledge and know-how we have acquired to apply to your real estate investing.

Regarding real estate education, we have taught everything from buying and selling it creatively as an individual or investor to core classes for licensing and passing real estate broker's exams. Recently we have co-authored a university course book on real estate principles and a book directed at real estate agents helping them work professionally with buyers and investors.

We have written four books currently available that we recommend you read to give you a broader background and more in-depth training to be more effective in your real estate investing in this crashing market. These include *Quick Cash in Foreclosures* (2004), *Make Money in Real Estate Tax Liens* (2005), *Make Money in Short-Sale Foreclosures* (2006), and *Make Money in Abandoned Properties* (2006). These books are all published by John Wiley & Sons. If you feel like a total newbie and have no money at all you could study and profit from our book *New Path to Real Estate Wealth, Earning Without Owning* (2003). To further help you sell your properties we have a best seller currently available from John Wiley & Sons: *How To Sell Your Home Without a Broker, Fourth Edition* (2004).

Our Philosophy

Our philosophy has always been that you need to be in control of your investments. Counting on a stock broker, investment adviser, accountant, general partner, or real estate investment fund leaves you completely out of control. When you are an actively engaged real estate investor, you

are the one calling the shots. You are the one responsible for your successes and failures.

As we are writing this introduction, the Bernie Madoff Ponzi scheme has unraveled and is in the process of destroying many people's lives. We promise you that you are the only person who can make you rich. Conversely, we promise you that you are the only person who can make you poor. Our mission is to provide you with the knowledge and information you need to be successful. And, if needed, we make ourselves available to you through our university HCIU or with fee-based consulting and partnering if you need that extra knowledge, push, information, or assistance.

Investing in Real Estate = High Net Worth

Investing in real estate is still the best vehicle to use to amass a high net worth. Do not be paralyzed into investment inaction by the negative media ranting that real estate is no longer a smart investment. Real estate has always been and always will be the small investor's surest way to become a multimillionaire.

The Peruvian-born economist Hernando de Soto got it right when he said the West became the economic world leader when our property laws and banking system gave us the ability to turn illiquid real estate (land) into liquid money. Cash and now cash and cash flow is king of the world. This book will show you how to become king or queen of your financial world.

How to Read This Book

We recommend you read this book in a particular way. Bring a lot of energy to your reading. This does not mean that you must necessarily read the book quickly, though that is fine with us. We want you to be excited about the material. Highlighters can be your best friend. Highlight items as you go. You could even color code your highlighting. Whatever it takes to enjoy and capture the information we are sharing with you. We want you to Win Going In as you read.

If you find yourself bogging down, stop reading. The material is designed to be comprehended in bursts. See if you can go from one insight to the next. You will become energized when you do this.

We would like to hear from you about your successes. Also, we want to hear what is working and what is not working for you. Please e-mail us at thetrustee@hotmail.com or contact us through our publisher, John Wiley & Sons.

We are available to partner with you on deals that you bring to us. We are available to help you put your deals together for a fee. If we do a partnership with you, we are jointly responsible for its success. If we consult with you on one of your deals, you are responsible for your success. Remember we have thousands of investors wanting to do business with us and thousands of students wanting to receive further education from us so please be patient and our staff will get you to us as soon as possible. When you e-mail please put the target date and topic in the subject line to assist us in sorting time priorities. Remember to include all your contact information and as much detail of the project as possible to expedite our response. Good luck and good deals!

—Chantal and Bill Carey

**THE ALL-NEW
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PART ONE

The Real Estate Market
Has Crashed

Pick a city in the United States: Boston, New York, Atlanta, Miami, Dallas, Chicago, Denver, Los Vegas, Phoenix, San Diego, Los Angeles, San Francisco, Portland, or Seattle. Everywhere in the country the real estate market is crashing—just as it is in other regions around the world. Prices in all 20 major metropolitan areas in the United States measured by the S&P/Case-Shiller Home Price Index are spiraling downward. Nationwide the index plunged 19.1 percent in the last year.

In 2008, in the United States alone, 3,000,000 homeowners received foreclosure filings on their homes. This represents 1 in 54 homes in the United States. According to a national foreclosure list company, more than 860,000 properties were repossessed by lenders last year. Many hundreds of thousands more were bought by real estate investors through short-sales or at the foreclosure auction. In the first six weeks of 2009, foreclosure proceedings began on another 296,000 homeowners according to the Center for Responsible Lending (a nonprofit organization focused on eradicating predatory lending practices).

At least 10 to 12 million households are facing foreclosure over the next four years. In the current economic downturn, 7 million to 8 million people could lose their jobs. They will not be able to make their mortgage payments. January 2009 foreclosure filings were up 18 percent from January 2008. Again, according to a national foreclosure list company 1 in every 466 households nationally received a foreclosure notice in January 2009.

Moody's Economy.com says that 13.8 million of the 52 million United States homeowners with a mortgage (27 percent) owe more on their mortgages than their homes are worth. This is what is known as being *underwater* with your mortgage.

Bank repossession rose 184 percent year-over-year. According to the National Association of Realtors (NAR) in the United States, 19 percent of the inventory of existing homes for sale in January 2009 was bank real estate-owned (REO) properties. This creates a huge downward pull on real estate prices. The median price of a single-family home in the United States was \$175,400 in December 2008 down 15.3 percent from a year ago. What happened to the housing boom?

Financial Derivatives Have Crashed the Real Estate Market

Financial derivatives have crashed the real estate market worldwide. A financial derivative is a contract between a buyer and a seller that derives value based on an underlying asset like a stock or a real estate mortgage. Poor quality mortgages were the underlying assets for trillions of dollars in high-cost derivatives. How did this happen?

A poor quality mortgage occurs when a borrower stops making monthly payments. Media attention has been focused on the subprime mortgage borrower. These were borrowers who were not qualified for A paper or prime mortgage loans. Banks loaned them money based on these borrowers' ability to breathe on a mirror and fog it up. These loans could be characterized as B, C, or D paper.

However, many borrowers of A paper and Alternative A (Alt A) paper have stopped making their mortgage payments, too. Alt A mortgages were given to borrowers who may have had good credit but had no long-term ability to make monthly mortgage payments. These were a version of NINJA loans. A NINJA loan means No Income, No Job, and (No) Assets.

Adjustable Rate Mortgages

Many A paper and Alternative A (Alt A) paper borrowers' inability to continue making monthly mortgage payments were exacerbated when the

mortgage came with an adjustable interest rate and/or adjustable monthly payment. After the initial teaser rate with its correspondingly low payment changed with the first rate adjustment triggering higher monthly payments, these borrowers could not afford to make their monthly mortgage payments.

Added to this banking debacle was the normal cyclical nature of the real estate market. Just as the top of the real estate cycle was being hit and a normal price leveling or price decline was occurring, the rates and payments on millions of real estate loans were adjusting upward.

Savings and Loan Crisis

In the 1980s, the United States experienced a crisis in the savings and loan industry. Cheap credit, nonexistent lending standards, and weak government regulation caused hundreds of savings and loan institutions to fail. Today, we have those same three factors at work plus two new ones.

The first new factor is that banking is no longer local. Banking is now global. Look what happened to the country of Iceland when its banks went under. The government collapsed. The second new factor is the packaging of mortgage debt into securities (derivatives) beyond the control of any government regulation.

From 1995 to 2005, Bank of America, JPMorgan Chase, and Citigroup became international players buying and selling stocks and bonds and managing assets such as mortgage-backed securities for big fees. This has been referred to as the universal bank model.

Acting Locally and Globally

These big banks were acting locally and globally. From 1995 to 2008, bank branches in the United States went from 81,000 to 99,000. This was a 22 percent increase. First-time home buyers and people wanting to pull equity out of their homes were encouraged to come in and borrow money. Unscrupulous mortgage brokers aggressively pursued predatory lending practices in order to maximize their profits.

In one of the most egregious cases of predatory lending practices discovered so far, Ray Vargas of Cerritos, California, was hit with

unconscionable lending fees, prepayment penalties, and interest charges. An investigation by msnbc.com showed that in a “21-month period in 2005 and 2006, Vargas’ home was refinanced five times through a total of six loans.”

According to msnbc.com his loan total went from \$213,555 to \$745,000. To access this \$531,445 in equity Mr. Vargas “paid at least \$123,237 in loan origination fees and prepayment penalties,” according to the report. He paid another \$60,000 in interest. This occurred as he was coping with the death of his wife of 57 years and her huge medical and nursing home bills. By the way, Mr. Vargas is 84. So what did the banks do with all these new loans?

Bundling

The banks then bundled together trillions of dollars of these mortgages and sold them to investors all around the world. Mortgages on properties in California, Nevada, Florida, or Rhode Island would become the underlying assets to financial derivatives sold to hedge funds in Paris, London, Singapore, or Shanghai.

In the past, credit had been extended based on the borrower’s ability to repay the loan. Now credit was being extended based on the lender’s ability to package a mortgage loan as a security instrument and sell it. Mortgage borrowers like Ray Vargas were just a means to an end. The big investment banks like Lehman Brothers, Merrill Lynch, Morgan Stanley, and Goldman Sachs saw how much money was being made and jumped into the game.

Wall Street Took over Main Street

Wall Street took over Main Street. These firms bought and sold mortgage-backed securities by borrowing astronomical amounts of money. In 2006, Goldman Sachs made a \$9.4 billion profit, which was the highest in Wall Street history. Morgan Stanley made a profit of \$7.1 billion. Their respective CEOs were paid bonuses of \$53.4 million and \$41.4 million.

Then toward the end of 2006 the housing market began to cool off. Subprime loans were the first to implode. This was the beginning of the end. During 2007 and 2008, all the players involved experienced massive

losses, as many borrowers in all types of mortgage categories stopped making their mortgage payments for various reasons. Banks now have \$5 trillion in nonperforming assets (potential losses) crushing their balance sheets.

AIG (American International Group)

AIG made a fortune selling insurance contracts to banks and hedge funds guaranteeing the value of the derivative contracts. By the fall of 2008, the United States Federal Reserve made the decision to rescue AIG. One hundred and fifty billion dollars later and the company that we have been told is too big to be allowed to fail is still failing. Without the government rescue the whole banking system would have collapsed under the domino effect because no bank's assets were worth the paper they were written on.

One portfolio of AIG assets the Federal Reserve holds is valued at \$20 billion of residential mortgage-backed securities. A second portfolio is valued at \$27 billion and consists of collateralized debt obligations, which are financial derivatives that combine slices of debt. These investment portfolios are made up of billions of dollars of toxic paper. Sorting out the toxic paper from the nontoxic paper is just one of the problems.

Financial Derivatives Are the Solution

However, noted expert and professor of economics at Yale University, Robert Shiller believes that financial derivatives are the solution to the current financial crisis. Financial derivatives are a risk management tool according to Shiller. He equates them to an insurance policy. "You pay a premium and if an event happens, you get a payment," says Shiller.

Robert Shiller is the Shiller of the S&P/Case-Shiller Home Price Index. Movement in this index can be traded on the Chicago Mercantile Exchange.

Shiller wants homeowners and lenders to be able to insure themselves against falling housing prices. He proposes doing this by using a version of a financial derivative. Let's look at an example.

Example

You buy a home for \$350,000. You make a 20 percent down payment of \$70,000. You borrow \$280,000 from your mortgage lender.

Home Purchase

Purchase price	\$350,000
Down payment	<u>-\$ 70,000</u>
Mortgage amount	\$280,000

You buy a derivative that is inversely related to the nearest regional S&P/Case-Shiller Home Price Index to your property. If the value of your property drops and by extension the Home Price Index drops, the financial derivative would go up in value and offset your loss.

Let's say the value of your home drops 30 percent or \$105,000 because of changing market conditions. Now your home is worth \$245,000.

Home Value Drops

Property value	\$350,000
Loss in value	<u>-\$105,000</u>
New property value	\$245,000

You are effectively underwater with your mortgage of \$280,000 being \$35,000 greater than the value of your property.

Underwater

Mortgage amount	\$280,000
New property value	<u>-\$245,000</u>
Underwater	\$ 35,000

Your financial derivative would go up in value from 0 to \$105,000.

This would recoup your \$70,000 down payment and your \$35,000 underwater amount.

Derivative Value

Down payment	\$ 70,000
Underwater amount	<u>+\$ 35,000</u>
Derivative value	\$105,000

Lenders Use Derivatives Locally not Globally

Lenders could do the same thing as their borrowers. By buying a derivative, the lender would have a hedge against having to foreclose and likely winding up owning property the lender is not interested in owning. If a borrower stopped paying on a mortgage loan the derivative would cure the deficiency.

It would also protect the lender from having to do a short-sale. A short-sale would require the lender to cram down the loan amount from \$280,000 to \$245,000 in order for the property to sell at the current market value. This would result in at least a \$35,000 loss to the lender.

Lender Loss

Mortgage amount	\$280,000
Cram down amount	–\$245,000
Lender loss	\$ 35,000

\$20 Trillion Housing Market

By having derivatives available for borrowers and lenders, the \$20 trillion housing market can become more liquid. Without derivatives there are very limited ways to unlock profit when the market falls. The stock market allows options and derivatives. This allows money to be made even when the market is falling.

This significantly increases the number of buyers and sellers in the stock market. More buyers and more sellers mean more liquidity. More liquidity means a better functioning market even in turbulent conditions.

History

In the 1920s, U.S. mortgage lending was a very simple financial transaction. If you wanted to borrow money to buy a home you went to your local bank. The bank gave you the money to buy your home and you gave the bank a promissory note and a mortgage contract.