

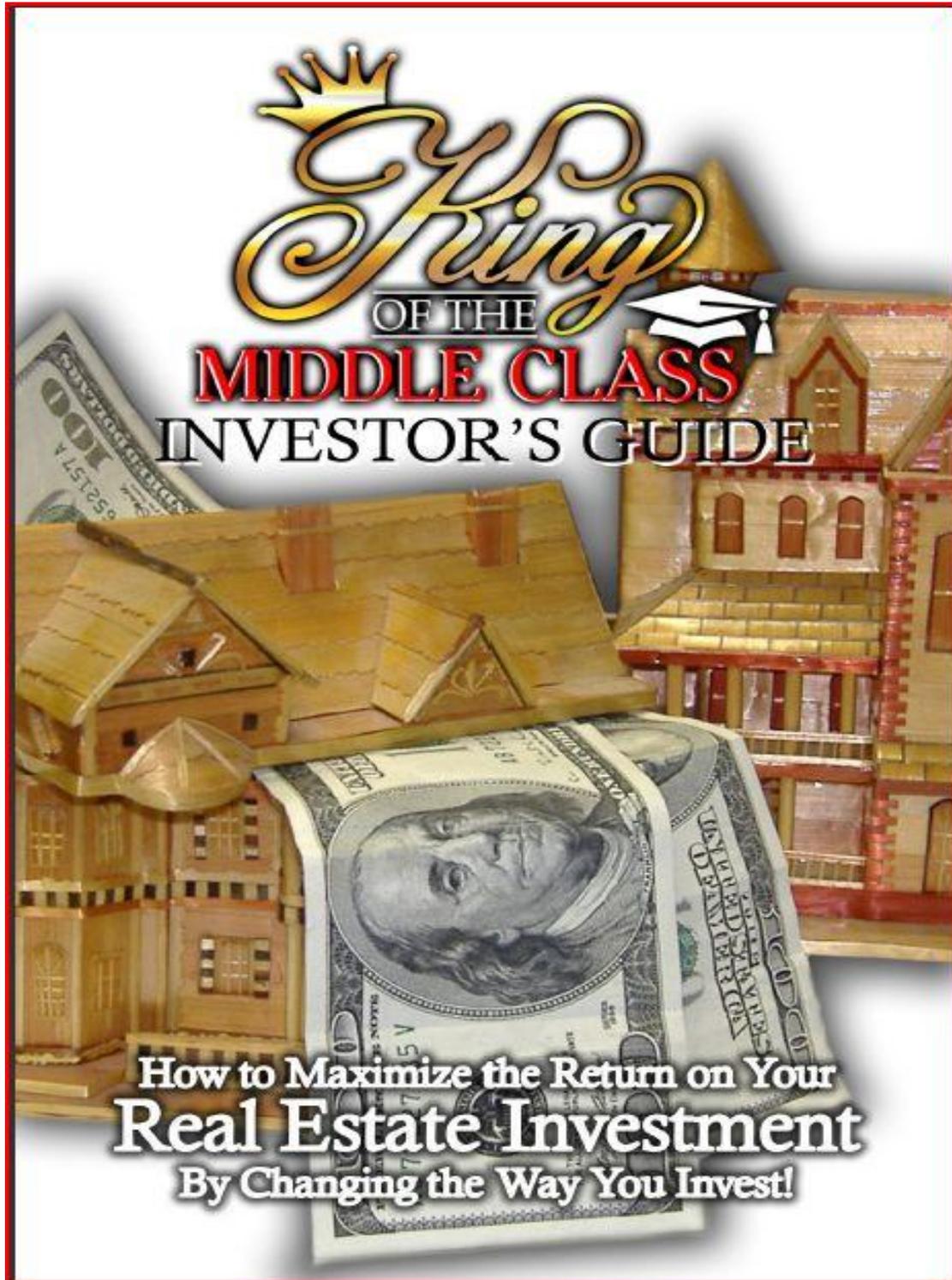
Researching Property Managers?

Go with a Proven Winner!

TRUST



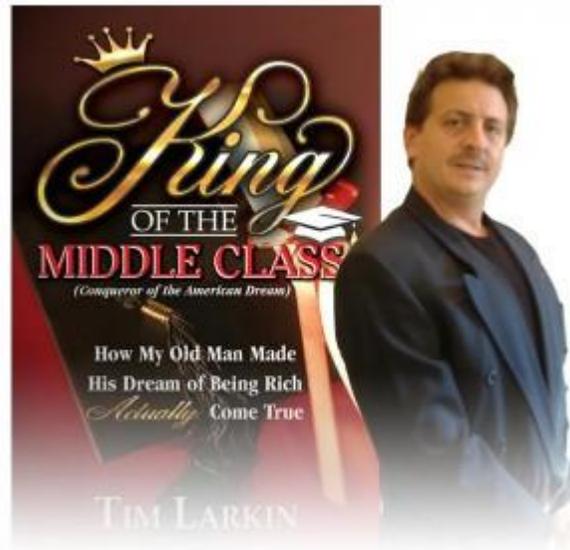
We wrote the Book on Rentals!



How to Maximize the Return on Your
Real Estate Investment
By Changing the Way You Invest!

Tim Larkin
King of the Middle Class
www.rkrnys.com

About The Author



[Tim Larkin](#) runs [Regal King Realty](#) a real estate company that specializes in rental investments & property management. Tim is a licensed real estate broker with an extensive financial background (series 7 & 66). He is an expert authority on buying real estate using a self directed IRA or 401 K & selling real estate using a 1031 Exchange.

Landlords retain him to build, manage and transfer their wealth.

I learned the rental and property management business from my dearly departed father, aka my old man. My old man and I were partners on over 54 rental properties together. While he was bedridden in a hospital I extracted all his real estate knowledge and wrote a Borders bestselling book called “King of the Middle Class”. This book should prove to you that I have the right experience and credentials to be your new property manager.

Enjoy the read.

As his mortal body lay dying, his perpetual soul came to life. The old man wanted to talk some more. He said, “Son, I don’t know what crime in life I committed to deserve such a harsh penalty as a death sentence.” I am not prepared for the journey, I am about to take. I don’t know what to pack for the afterlife trip that I am about to embark on. I am afraid no training in the universe can prepare a man for such an odyssey. I will soon, rather reluctantly, have the opportunity to experience one of life’s most horrifying events; physical death of the host body that houses my perpetual soul. I will soon be able to answer the age-old question of what happens when you die. I will cease to exist in your world. I will be a non-event, like I never happened. In time, no one alive will ever even know I was here. My jokes will be forgotten; my life stories lost, and I will fade away from anybody’s memories. The wonderful experiment called life will be over for me. One hundred years from now, when no relatives, friends, or family members are left that knew me; I won’t even be talked about. I will be a forgotten name on an unvisited tombstone, silenced by death. My pass in life will be expired. Eventually everyone I touched in life will no longer be around to keep the memory of my life alive.

“I implore you, as my son, to make a promise to me. Promise to keep the memory of my life alive so that the time I spent in this wonderful world wasn’t a worthless, trivial, forgotten event. I won’t be able to carry out this mission where I am going; I pass the torch to you on this one. I hope you love me enough to carry out this mission. I just want to be remembered by your children to be and possibly, dare I dream, their children-to-be and possibly, dare I dream, their children-to-be. I will donate whatever time is left in me to help you do this; it’s not like I have somewhere important to go. My only dream for what is left of my life is to be fondly remembered.

“The illusion of my monetary dreams has been evaporated; money is just meaningless, worthless, valueless paper to me now. I won’t need it where I am going. I just don’t want my life and the rich things I did in life to become as devalued as the money I leave behind for you after I check out. You are my greatest treasure. I know now, from this vantage point, that the greatest assets in life one can accumulate are people not money. I now know the only reason, I amassed a fortune in monetary gains is because I placed a higher value on the truly valued assets in life—the people that helped me along the way. My last dream before I leave this planet is for you to promise me that you will do everything in your power to keep the memory of my life alive in the hearts and souls of your children to be. It is your job to pass on this family tradition. I will leave you all the money possible to carry out this endeavor, but ultimately only your love and respect for me will make this dying man’s dream realized. Son, don’t let me die in vain.” He nodded off.

The old man awoke from his dream and proclaimed, “Son do you know what happens to your dreams when you die?”

I said, “Real dreams never die, Dad; they are immortal. They are impervious to time. There is no limit or boundary line for a real dream because there is no limit to the imagination that creates the dream. Your imagination is infinite. Nothing can stop a real dream from happening, not even physical death. Real dreams survive many deaths. You can ask Martin Luther King Jr., when you meet him, he’ll tell you. Why do you think OJ Simpson was exonerated? Because he didn’t care how much money it cost to realize his dream of freedom. He spent his entire fortune and then some on a Dream Team that helped him realize his dream. He is living proof that dreams do come true. Dad, I am your dream team.

“Dad, I will make your last dream come true. I will prove to the world that dreams really do come true. My dream in life will be making sure your last dream in life becomes everyone else’s reality. I won’t do it for me, Dad. I’ll do it for you. I figure I owe you that respect. I will spread your word, like a loyal servant. I will not fail in my mission. I will rescue the starving minds of America from their poor thoughts and feed them with your rich wisdom. Most people have a Plan B, a back-up plan, just in case the real plan doesn’t work out. They have something to fall back on, like an aspiring actress has a waitress job, I too have a Plan B. My Plan B is not to screw up Plan A, because my plan B is my Plan A. I learned from you, “The best way to protect your future is to create your future with the endless power of your dreams”. My Plan B is to properly carry out Plan A, because my Plan B is my Plan A. All or none, the man on a mission only knows one speed, forward, no matter what adversity or doubts or setbacks, nothing compromises the integrity of the mission. The mission will be accomplished no matter what the odds or personal sacrifices.”

Translation: There is no plan B on this one, Dad. My plan B is not to mess up Plan A. Plan A is Plan B. Plan A is the only plan. I am only focused on accomplishing one thing in life, and one thing only: properly executing Plan A. I am a marksman with only one bullet in the chamber; this is my one shot, and I am taking it for you, Dad. I am stepping up to the proverbial “plate” and swinging my idea at America. I am not going to borrow your dream and pretend it is mine. NO! I am going to take your dream and make it my real dream. I will inherit your dream along with your money and use it to make my dream of you being fondly remembered, a reality.

“It is my dream; no one can steal it from me. It is not for sale. Dreams are earned, not bought. No amount of money in the entire universe could stop me from accomplishing my dream. The message will be delivered. I am as unstoppable as a fully packed eighteen-wheeler barreling down a slick hill with no brakes. My whole life was preparation for this journey. I will prove, ‘If you can dream it, it can be done.’

In my mind, my dream is already accomplished; I am just looking back from my future and marveling at how I wrote a book and accomplished my dream. That’s how sure I am that this dream will come true. It is a foregone conclusion. It is a done deal it’s history already. I am just a time traveler who wanted to go back in time and relive it again. My wild dream will become everyone else’s calm reality. You should get accustomed to the fact, that it is already done, Dad, because I am not going away until I live to see my dream successfully fulfilled.

My old man thanked me in advance for conquering my errand—our dream—and reminded me of one very important thing: real dreams are only accomplished when you discard your old notion that “Seeing is believing” and replace it with the correct notion that “Believing is Seeing.”

I replied, “Yes, I know, and that is why I will do one thing for you in the future, Dad.” I will gather all your grandchildren, the ones who knew you and the ones who knew of you, and we will ceremoniously correct the epitaph on your tombstone in Laurel Cemetery to properly reflect my conviction to grant you your last Dream.

Your Epitaph, for the entire world to see, will read:

Henry G Larkin

Still Living

His Dreams

The old man mused, “So you are going to write a book about me, huh?”

I said, “Absolutely, it’s the only way I could realistically think of to make my dream truly come true.”

What have I done in life that warrants such kudos?” the old man asked.

I said, “Number one, you performed a miracle; you created me, and number two, you accomplished a dream that eludes many struggling Americans—the dream of financial freedom”. I will share your accomplished dream with fellow Americans and accomplish my own dream at the same time, because, Dad, dreams do come true. I will prove it. I will show fellow Americans, in your memory, what this country was really built on; the backs of tireless dreamers like you. Dad, I will earn your place in history by showing Americans that dreams do come true. Once people understand that dreams really do come true, maybe a new revolution of thinking can sweep this great country and immobilize others to aspire as far as their dreams conjured in their vivid imaginations will take them. All Americans will benefit from our example.

My old man had the desire and tenacity to accomplish the dream of being truly rich, rich in thought and rich in monetary gain. And I am here to show you how to do it as well. All I ask is for you to fondly remember my old man after this book helps you conquer your dream of being truly rich.

The old man said, “Remember, Tim, always be a friend; never talk above, below, or at people. Enrich your life experience and talk with people because:

‘The true mark of a friend is to be genius enough to have the ability to take large chunks of complicated subject matter and translate the meaning into small pieces of understandable thoughts that can be easily digested by all,’ or as Albert Einstein used to say, ‘Everything should be made as simple as possible, but not simpler.’

As Chairman of the Board of Regal King Realty based in West Sayville, New York it is incumbent upon me to pay respectful homage to my mentor and fulfill an obligation I made to him on his deathbed. I told my old man that I wouldn’t let his ideas die with him. I promised that I would preserve his legacy by sharing his teachings with fellow Americans. In essence, I am here to immortalize my mentor and his ideology by recruiting you as my protégé to spread his message and profit from his beliefs. I am your guide to his kingdom of knowledge. I am the son, in-line to the throne, and I am here to assume my position as your mentor, and to teach you how my old man conquered his dream of retiring early by properly investing in real estate, and became a “King of the Middle Class.”

The old man said there are four reasons why you should invest in Real Estate:

- 1) **Forced Equity**
- 2) **Market Equity**
- 3) **Tax write-offs**
- 4) **Positive cash flow**

1) "Forced Equity" - Automatic monthly windfall

The old man said, before you can fully appreciate the concept of "forced equity" you must have a general understanding of how a mortgage loan works and what amortization is. He cited a typical example: You find a house for sale for \$260,000, you put 20% down which is \$52,000 and now you are looking for money to pay for the balance of the purchase price remaining that is due the seller of this house in this case \$208,000. The best way to get this money (208,000) is to borrow it. You go to your local mortgage broker or a bank and they check out your credit, income and assets and if everything checks out okay; you meet their underwriting guidelines and they agree to lend you money, Bingo You are Approved!! You are now entitled to rent their money for a specific amount of time and at a predetermined rate of rent called interest. You then have the privilege of going to a closing where you will pay the lender any fees associated with renting this money commonly called closing costs. At the closing you will be given a HUD one statement; basically a itemized receipt for all the money it cost you to rent the money you needed to pay the seller for the privilege of buying their house.

At the closing you will sign hundreds of legal documents; banks take lending their money out pretty seriously, its not like the old days where you shook hands and blindly trusted each other. The old man snapped, "Corruption killed that honesty game ". Now everything in real estate according to the Statue of frauds has to be in writing. The most consequential of these written documents are the Mortgage and the Mortgage Note. These documents clearly lay out in writing the terms and conditions of borrowing this money.

Contrary to popular opinion the bank or licensed mortgage banker does not give you a mortgage on a property; they give you rented money, you give the lender a mortgage, its like a pledge, an IOU, you pledge to pay back the lender based on the terms and conditions of a mortgage note that you also signed at the closing; if you do not live up to this pledge the documents you signed gives the lender the legal right to force you, by court order if necessary, to abide by the terms and conditions you agreed to , as evidenced by your signature, or lose your home. Simply Put, you don't Pay you don't stay. The mortgage that the lender records in the County Clerk's Office (so it is public information) is collateral for the repayment of the rented money. If you do not pay the rent per month (the mortgage payment) the lender can foreclose on the house. Translation: the lender can sell the house through a legal process called foreclosure to recover rent monies (interest) due them under the terms of the Mortgage Note. The Mortgage Note on the other hand is the actual evidence of the debt owed. The mortgage note spells out in no uncertain terms how much money you rented or borrowed and how much you will pay back usually on a monthly basis and for how long a term (10,15,20,25,30,40 years). The note is never recorded, only it's cousin, the mortgage gets the privilege. I guess the concept being why should the whole world know what rent you pay for the honor of borrowing money. The old man said, the lenders like this privacy policy as well it makes it harder for competitors to steal their yields through refinancing. If Dum Dum Lending Corp. recorded the mortgage note; all their competitors would know exactly what price to charge to steal their business- the business of renting money. If Dum Dum in it's infinite wisdom recorded a mortgage note showing that it

was charging the borrower 8% interest (rent) to borrow its money it would not take long for a competitor, willing to take less rent (interest) say 7% to steal it by refinancing the debt and paying off Dum Dum lending corp. The lenders don't like to lose their customers; they spend a lot of money on advertising and marketing expenses to get these customers. The note, not being recorded protects the lenders from easily stealing each other's business. If the interest rates or rent people paid to borrow money was public information then the bankers would be forced (due to competition) to work on leaner and meaner profit margins; not good for their bottom line. It is better for the entire banking industry that the interest or rent people pay remain a guarded secret, like how today's fico scores that all lenders use is calculated. The old man wasn't around for fico scores, but if he was I am sure he would have demanded that his tenants or as he would call them his "*Pension Walkers*" pay him on time so as to preserve that high fico score, guaranteeing the maximum borrowing power with the lowest rate.

The other natural reason for not divulging interest rate charges is that people would use this information to judge each other. If someone knew you paid a high interest rate (rent to borrow money) they would assume one of three things a) you were stupid for paying a high rate when you could easily refi or b) you were paying a high rate because you were too lazy to do the paperwork required to lower it or c) you had bad credit and this rate is the best you can get with your credit. High interest rate people would be outcasts; the bankers wouldn't want this to happen to their best paying customers, its bad for business.

The note usually contains another protective clause that prevents the borrower from switching lenders for the first 12months; it is called the pre-payment penalty. If you obtain a loan at 9 % interest (rent to borrow) on April 1st and 2 months later another lender offers you a 8% rate – you can drop your first lender but they will charge you a departure fee for the privilege of paying off this debt earlier than they could make any real money off of you, this privilege usually runs around 5 % of unpaid principal balance owed. On a \$208,000 loan this privilege would cost you \$10,400 (5% of 208,000). You could take the lower rate loan and pay the legal extortion (10,400) or you can refrain from refinancing until pre-pay period is over (usually one year, but certain California lenders have three & five year pre-pays) and hope rates are still low enough to justify switching companies. One strange advantage of an adjustable rate mortgage is that there is no pre-payment privilege attached to it. Go figure. I wonder why? I guess its because the lenders could keep raising your rate (the rent they charge you to borrow their money) through dubious indexes and keep you paying the rate by holding the pre-pay departure fee over your head. The customer would be forced to choose between two evils- a higher payment per month, when the rate adjusts or a very high bail out fee called the pre-pay.

These notes are usually stored in very safe places, as they are the only Proof of the IOU existing between mortgagor (borrower) and mortgagee (lender). The note is only valid with original signatures, copies are meaningless. If the lender loses the original note theoretically the mortgagor (the person renting the money) can challenge the validity of the debt. The mortgagee (lender) uses the note as a back up to the recorded Mortgage- If the house is sold to recover the money owed (foreclosure) and the lender does not receive all monies due; they can sue you (the borrower/renter of money) personally for the money owed. This is called a deficiency judgment. Translation: If you default on the loan and the lender sells your house based on the mortgage you gave to them at public Auction through the foreclosure process and the lender does not net enough money to satisfy all monies owed under the note you signed they can and will personally sue you via a deficiency judgment for the balance remaining.

As a side note, mortgage companies/banks require escrow accounts for payments of property taxes and homeowners insurance because non-payment of these expenditures would endanger the collateral (the house) that you pledged as security for repayment of loan. For example, if the house burned down and there was no fire insurance on the property naming the lender as loss payee, the lender would have no protection from a default on the loan. They would be stuck with a burned out shell as collateral instead of a fixed up home. If the property taxes aren't paid on the property, the county could after say 3 years foreclose on the property and wipe out the mortgage loan so the lenders make damn sure your taxes are paid ;(property taxes are a superior lien they can wipe out a mortgage lien regardless of recordation date- if mortgage was recorded prior to tax debt doesn't matter- taxes have to be paid –the county would record a tax deed and forcibly take property regardless of mortgage loan on property) if you fail to pay the property taxes smart lenders pay them (the mortgage docs you signed allows them to) and add payment to principal balance remaining on your loan.

Translation: A Mortgage / Mortgage Note is like any other contract- it is only as good as the quality & integrity of the people that sign these legally binding documents. In an ideal world the mortgage companies would never need protective documents like a Mortgage or Mortgage Note to insure they get paid; a handshake would do, but in the real world unforeseen events like losing a job, death, divorce, relocation & bankruptcy make these protective measures a necessity.

The Note that you signed at closing clearly spells out in plain English how much money you rented (borrowed), how much you will have to pay the lender per month to rent (borrow) the money (affectionately called interest) and for how many years you will pay this rent (interest) to the lender. For example you borrow \$208,000 @ 7 % interest for 30 years (360 monthly installments). The Note you sign at closing would clearly state that you rented \$ 208,000 from the lender, and that you will pay the lender \$1383.83 in equal monthly installments for the privilege of using their money, and you will pay this rent (interest) for 360 months (30 years) at which time the loan will be paid in full. This concept is known as amortization. Once the loan is paid in full, it is important to get a SAT (a legal document from the lender acknowledging that loan has been paid in full and your obligation to the lender is satisfied). Once you obtain the SAT it is imperative that you spend the extra dough (100-200 bucks) to record the SAT in the county Clerks office, so the whole world knows your debt is absolved, no questions asked. The old man said I can't tell you how many times I have saved a closing by picking up an original SAT, haphazardly tossed in a drawer, the owner unawares of the legal importance of this document. The SAT is the only official legal proof that the loan has been paid in full, so if you want to avoid a major title problem whenever you refi or sell, make sure a) if you paid off your loan you get a SAT from the lender (some lenders take 2-3 months to forward papers)(in a refinance the title company usually , for a fee takes care of this) and b) after you get SAT from lender you promptly invest a few bucks and record it. The old man was adamant on this point, he said if you lose the original SAT they sent you it could take weeks to replace it and if your lender went out of business (like the scammy fly by night home improvement lenders)or got bought out or merged with another lender it could take months or years to solve the problem . You could even be forced to spend thousands on an attorney to legally extinguish your obligation through the courts. Translation: If you want to save lots of time and money and mental energy give your SAT the respect it deserves and record it. (PS- you always knew when the old man recorded his SAT's- he always threw a party- only his closet friends and family knew it was a burn-the-mortgage party).

The old man said, now that you have a mortgage loan you should become familiar with the concept of amortization. Basically amortization means you make one equal payment to a lender on a monthly basis for a set number of years until loan is paid in full. This equal payment is broken down into principal and interest payments. The interest payment column goes down each month and the principal column goes up each month. Translation: Even though you are making the same constant equal payment month after month the amount of each payment that goes toward principal payback of loan and interest charged to use the money changes every month; You owe less and less interest each month because the principal balance that is being used to calculate interest owed is being paid off.

The trick to this concept is to figure out what the equal payment per month should be based on how much you borrowed and how much interest you are being charged to borrow this money and for how long you need this borrowed money. For example if you need to borrow \$208,000 @ 7 % for 360 months (30Yrs.) What would be the equal monthly payment you would have to pay, over a 30 year or 360 month period of time to pay back the loan plus all interest owed to lender? What would be the equal monthly payment if you wanted to pay back the loan over a 15 year or 180 month period of time? Well thank god some financial wizards got together and figured all this out for us. They created financial amortization charts. Basically, these charts are designed to tell you how much per thousand it would cost you per month to borrow (rent) money at different interest rates and different periods of time. To figure out your amortized payment, all you do is take your loan amount (which for our example will be \$208,000) divide it by 1000 (which is 208,000 divided by 1000= 208) and then use the chart with this number (208) for any interest rate or term. If you were borrowing 208,000 @ 7 % for 30 years, you would go to the left hand of chart and find the interest rate , which in our case is 7% , and then you would go across the 7% column and find the per thousand multiplier that corresponds to the term of the loan, (10,15,20,25,30) which in our case is 30 years or 6.65 per 1000. Now take your 208 times it by 6.65 and voila you got your monthly principal and interest payment; \$ 1383.20 per month. This is the equal payment you would have to make each and every month for the next 30 years, in order to pay back the lender a 7 % yield on the loan plus pay back the entire principal balance that you borrowed.

EQUAL MONTHLY PAYMENT TO AMORTIZE A LOAN OF \$1,000

TERM	10	15	20	25	30
INTEREST RATE					
6.0	11.10	8.44	7.16	6.44	6.00
6.500	11.35	8.71	7.46	6.75	6.32
7.0	11.61	8.99	7.75	7.07	6.65
7.125	11.68	9.06	7.83	7.15	6.74
7.250	11.75	9.13	7.91	7.23	6.83
7.375	11.81	9.20	7.98	7.31	6.91
7.500	11.87	9.27	8.06	7.39	6.99
7.625	11.94	9.35	8.14	7.48	7.08
7.750	12.01	9.42	8.21	7.56	7.17
7.875	12.07	9.49	8.29	7.64	7.26
8.0	12.13	9.56	8.36	7.72	7.34
8.125	12.20	9.63	8.45	7.81	7.43
8.250	12.27	9.71	8.53	7.89	7.52

Tim Larkin
King of the Middle Cass
www.rkrnys.com

8.375	12.34	9.78	8.60	7.97	7.61
8.500	12.40	9.85	8.68	8.05	7.69
8.625	12.47	9.93	8.76	8.14	7.78
8.750	12.54	10.00	8.84	8.23	7.87
8.875	12.61	10.07	8.92	8.31	7.96
9.0	12.67	10.14	9.00	8.39	8.05
9.125	12.74	10.22	9.08	8.48	8.14
9.250	12.81	10.30	9.16	8.57	8.23
9.375	12.88	10.37	9.24	8.66	8.32
9.500	12.94	10.44	9.32	8.74	8.41
9.625	13.01	10.52	9.41	8.83	8.50
9.750	13.08	10.60	9.49	8.92	8.60
9.875	13.15	10.67	9.57	9.00	8.69
10.0	13.22	10.75	9.65	9.09	8.78
10.500	13.50	11.06	9.99	9.45	9.15
11.0	13.78	11.45	10.41	9.90	9.62
11.500	14.06	11.69	10.67	10.17	9.91
12.0	14.35	12.01	11.02	10.54	10.29
12.500	14.64	12.33	11.37	10.91	10.68
13.0	14.94	12.66	11.72	11.28	11.07
13.500	15.23	12.99	12.08	11.66	11.46
14.0	15.53	13.32	12.44	12.04	11.85
14.500	15.83	13.66	12.80	12.43	12.25
15.0	16.14	14.00	13.17	12.81	12.65

**Note- The above figures are estimates only- exact figures are calculated by pre programmed computers- For example our \$208,000 loan @ 7 % for 30 years comes out to exactly \$1383.83 per month (as per MLS computer)- but according to the chart 7 % for 30 years is 6.65 per 1000 or 6.65 X 208= 1383.20. The computer is much more accurate- in our example, the per thousand multiplier is 6.653. 6.653 X 208= 1383.83

(www.freemortgageanalyzer.com- web site that can do calculations for you)

Sample Amortization Chart Exercises

- 1) What is your equal monthly payment if you borrow \$208,000 @ 6% for a term of:
 - 10 yrs _____
 - 15 yrs _____
 - 20 yrs _____
 - 25 yrs _____
 - 30 yrs _____

- 2) What is your equal monthly payment if you borrow \$208,000 for 15 yrs at an interest rate of:
 - 6% _____
 - 7% _____
 - 7.375% _____
 - 14% _____
 - 11% _____
 - 9.125% _____
 - 8.750% _____

3) What is your equal monthly payment if you borrow money @ 7 % for 30 years for a loan amount of:

- \$100,000 _____
- \$125,000 _____
- \$258,000 _____
- \$97,000 _____
- \$456,550 _____
- \$238,775 _____

The old man instructed, an amortized loan by design is a self liquidating loan, a loan designed to pay itself off and that's why each equal monthly payment is divided into 2 parts - a) interest payment to bank (the banks profit per month) and b) principal payment to bank (our profit per month- the equity caused by the monthly lowering of the principal balance remaining on our loan- the monthly windfall the old man affectionately called "Forced Equity", the Landlord's Forced savings plan) Your mortgage payment always remains the same(in our case \$1383.20 for 360 months (30 years)) , how much of that payment goes toward principal and interest payments changes every month ; because every month as you slowly chip away at the principal balance owed , you pay less & less interest because the principal balance that you use to calculate your interest payment is decreasing month by month.

The old man said, "Now get out your calculator and lets Go Figure", " forced equity " is the by product of amortization and the only way you will understand amortization is to experience amortization. Lets do an amortization exercise, lets borrow \$208,000 @ 7% for 10yrs /15 yrs / 20yrs / 25yrs & 30yrs – same rate of interest but different payback terms. We will manually, using our calculator, figure out the first 12 amortized payments of principal & interest on all 5 loans. We will do by hand, for purposes of learning and understanding, what a computer can do in seconds; create a one year amortization schedule of payments for these loans. Lets Begin.

You borrow \$208,000 at 7 % interest for 120 months (10yrs) –What is the monthly payment? You go to the chart and find the interest rate first, in this case it is 7.0 and then you find the multiplier per thousand for the term of loan, in this case 10 years is 11.61 per 1000 dollars borrowed. Now it is simple math $11.61 \times 208 = \underline{\$2414.88}$ per month. This is the monthly payment you must tender to the lender to pay back this loan with interest in a 10 year time period. Total payments to lender in 10 years= $\$2414.88 \times 120\text{months} = \underline{\$289,785.60}$. Total profit to bank $\$289,785.60$ minus $\$208,000$ original principal owed = $\underline{\$81,785.60}$ (this is how much money the bank would make if you kept the loan for the full 10 years. After 10 years you would owe the bank nothing; the entire principal balance was eliminated month-by-month, year-by-year, through the process of amortization. Now lets calculate our forced equity for the first month, by breaking down the amortized mortgage payment of $\$2414.88$ per month into principal & interest. (As per ***Note under chart -for our illustration we will use the more accurate computer generated number for $\$208,000 @ 7\% 10 \text{ yrs} = 2415.06$ per month) How do we calculate what portion of this mortgage payment (2415.06) goes toward interest; the banks profit and how much goes toward reducing the principal balance owed, our profit or "forced

Equity”. Its simple math. You start with the principal balance. You only pay interest on what you owe, so your first interest payment you would pay 7% on the full \$208,000, which is $208,000 \times 7\% = 14,560$ per year, 14,560 divided by 12= **\$1213.33** interest for the month. This is the profit the bank makes the first month on the job.. If the amortized payment per month is \$2415.06 (adjusted per computer accuracy), its simple subtraction $2415.06 - 1213.33 = 1201.73$; this represents the portion of your payment that the lender uses to pay down your debt . You now owe your lender \$208,000 minus 1201.73. This **\$1201.73** for this first month represents your “forced equity” profit. The first month of our loan the 2415.06 mortgage payment was broken down as follows:

\$ 1213.33 – interest to lender (banks profit)

\$ 1201.73- principal payment on loan to reduce debt (our forced equity profit)

By month #2 you do not owe \$208,000 any more, you owe \$208,000 minus \$1201.73 or \$206,798.27. This is the new principal balance, and since you only pay interest on what you owe your 2nd interest payment will be 7 % of 206,798.27 not 208,000. To calculate the 2nd month interest we times \$206,798.27 by 7 % equaling 14,475.88 per year divided by 12 equals **1206.32** interest owed for month. This is the profit the bank makes the second month on the job. The first month we owed the lender **1213.33** interest for the month because we owed the lender \$208,000, the 2nd month we owed the lender **\$1206.32** interest for the month (a little less) because the principal balance that we used to tabulate interest owed has been reduced from \$208,000 to \$206,798.27. Since the amortized monthly mortgage payment of 2415.06 doesn’t change , it’s simple subtraction $2415.06 - 1206.32 = 1208.74$, this represents the portion of your payment that the lender uses to pay down your debt owed. You now owe your lender 206,798.27 minus \$1208.74. This **\$1208.74** represents your 2nd month of “forced equity” profit. Each month our “forced equity” profits go up and the mortgage company’s rent (profit) for using their money goes down because we owe them less and less as the months and years go by. The second month of our loan the 2415.06 mortgage payment was broken down as follows:

\$ 1206.32- interest to lender (banks profit)

\$ 1208.74- principal payment on loan to reduce debt (our forced equity profit)

By month # 3 you do not owe \$206,798.27 any more, you owe \$206,798.27 minus \$1208.74 or \$ 205,589.54. This is the new principal balance, and since you only pay interest on what you owe your 3rd interest payment will be 7 % of 205,589.54 not 206,798.27. To calculate the 3rd month interest we times \$205,589.54 by 7 % equaling 14,391.27 per year divided by 12 equals **1199.27** interest owed for the month. This is the profit the bank makes the third month on the job. The second month we owed the lender **1206.32** interest for the month because we owed the lender \$206,798.27, the third month we owed the lender **\$ 1199.27** interest for the month (a little less) because the principal balance that we used to tabulate interest owed has been reduced from \$206,798.27 to \$205,589.54. Since the amortized monthly mortgage payment of \$2415.06 doesn’t change, its simple subtraction $2415.06 - 1199.27 = 1215.79$; this represents the portion of your payment that the lender uses to pay down your debt owed. You now owe your lender 205,589.54 minus **1215.79**. This **\$1215.79** represents your 3rd month of “forced equity” profit. The third month of our loan the 2415.06 mortgage payment was broken down as follows:

\$ 1199.27- interest to lender (banks profit)

\$ 1215.79- principal payment on loan to reduce debt (our forced equity profit)

By month #4 you do not owe \$205,589.54 any more, you owe \$205,589.54 minus \$1215.79 or \$204,373.75. This is the new principal balance, and since you only pay interest on what you owe your 4th interest payment will be 7 % of \$204,373.75 not \$205,589.54. To calculate the 4th month interest we times \$204,373.75 by 7 % equaling 14,306.16 per year divided by 12 equals \$1192.18 interest owed for the month. This is the profit the bank makes the fourth month on the job. The third month we owed the lender \$1199.27 interest for the month because we owed the lender \$205,589.54, the 4th month we owed the lender \$1192.18 interest for the month (a little less) because the principal balance that we used to calculate interest owed has been reduced from 205,589.54 to 204,373.75. Once again the amortized monthly mortgage payment of \$2415.06 doesn't change, its simple subtraction 2415.06 minus 1192.18 equals 1222.88, this represents the portion of your payment that the lender uses to pay down your debt owed. You now owe your lender 204,373.75 minus 1222.88. This \$1222.88 represents your 4th month of "forced equity" profit. The fourth month of our loan the 2415.06 mortgage payment was broken down as follows:

\$1192.18- interest to lender (banks profit)

\$ 1222.88 – principal payment on loan to reduce debt (our forced equity profit)

By month # 5 you do not owe \$204,373.75 any more, you owe \$204,373.75 minus \$1222.88 or \$203,150.87. This is the new principal balance, and since you only pay interest on what you owe your 5th interest payment will be 7 % of \$203,150.87 not \$204,373.75. To figure out the 5th month interest we times \$203,150.87 by 7 % equaling 14,220.56 per year divided by 12 equals \$1185.05 interest owed for the month. This is the profit the bank makes the 5th month on the job. The 4th month we owed the lender \$1192.18 interest for the month because we owed the lender \$204,373.75, the 5th month we owed the lender \$1185.05 interest for the month (a little less) because the principal balance that we used to calculate interest owed has been reduced from 204,373.75 to 203,150.87. Since the amortized monthly mortgage payment of \$2415.06 doesn't change, its simple subtraction 2415.06 minus 1185.05 equals 1230.01; this represents the portion of your payment that the lender uses to pay down your debt owed. You now owe your lender \$203,150.87 minus \$1230.01. This \$1230.01 represents your 5th month of "forced equity" profit. The 5th month of our loan the 2415.06 mortgage payment was broken down as follows:

\$ 1185.05- interest to lender (banks profit)

\$ 1230.01- principal payment on loan to reduce debt (our forced equity profit)

By month # 6 you do not owe \$203,150.87 any more, you owe \$203,150.87 minus \$1230.01 or \$201,920.86. This is the new principal balance, and since you only pay interest on what you owe your 6th interest payment will be 7 % of \$201,920.86 not \$203,150.87. To figure out the 6th month interest we times \$201,920.86 by 7 % equaling \$14,134.46 per year divided by 12 equals \$1177.87 interest owed for the month. This is the profit the bank makes the 6th month on the job. The 5th month we owed the lender \$1185.05 interest for the month because we owed the lender \$203,150.87, the 6th month we owed the lender \$1177.87 interest for the month (a little less) because the principal balance that we used to calculate interest owed has been reduced from \$203,150.87 to \$201,920.86. Since the amortized monthly mortgage payment of \$2415.06 doesn't change, its simple subtraction 2415.06 minus 1177.87 equals 1237.19; this represents the

portion of your payment that the lender uses to pay down your debt owed. You now owe your lender \$201,920.86 minus \$1237.19. This \$1237.19 represents your 6th month of “forced equity” profit. The 6th month of our loan the 2415.06 mortgage payment was broken down as follows:

\$ 1177.87- interest to lender (banks profit)

\$ 1237.19- principal payment on loan to reduce debt (our forced equity profit)

By month # 7 you do not owe \$ 201,920.86 any more, you owe \$201,920.86 minus \$1237.19 or \$200,683.67. This is the new principal balance, and since you only pay interest on what you owe your 7th interest payment will be 7 % of \$ 200,683.67 not \$201,920.86. To figure out the 7th month interest we times \$200,683.67 by 7 % equaling \$14,047.86 per year divided by 12 equals \$ 1170.65 interest owed for the month. This is the profit the bank makes the 7th month on the job. The 6th month we owed the lender \$1177.87 interest for the month because we owed the lender \$201,920.86, the 7th month we owed the lender \$1170.65 interest for the month (a little less) because the principal balance that we used to calculate interest owed has been reduced from \$201,920.86 to \$ 200,683.67. Since the amortized monthly mortgage payment of \$2415.06 doesn't change, its simple subtraction 2415.06 minus 1170.65 equals 1244.41; this represents the portion of your payment that the lender uses to pay down your debt owed. You now owe your lender \$200,683.67 minus \$1244.41. This \$1244.41 represents your 7th month of “forced equity” profit. The 7th month of our loan the \$2415.06 mortgage payment was broken down as follows:

\$ 1170.65- interest to lender (banks profit)

\$ 1244.41- principal payment on loan to reduce debt (our forced equity profit)

By month #8 you do not owe \$ 200,683.67 any more, you owe \$200,683.67 minus \$1244.41 or \$199,439.26. This is the new principal balance, and since you only pay interest on what you owe your 8th interest payment will be 7 % of \$ 199,439.26 not \$200,683.67. To figure out the 8th month interest we times \$199,439.26 by 7 % equaling \$13,960.75 per year divided by 12 equals \$1163.40 interest owed for the month. This is the profit the bank makes the 8th month on the job. The 7th month we owed the lender \$ 1170.65 interest for the month because we owed the lender \$200,683.67, the 8th month we owed the lender \$ 1163.40 interest for the month (a little less) because the principal balance that we used to figure out interest owed has been reduced from \$200,683.67 to \$ 199,439.26. Since the amortized monthly mortgage payment of \$2415.06 doesn't change, its simple subtraction 2415.06 minus 1163.40 equals 1251.66; this represents the portion of your payment that the lender uses to pay down your debt owed. You now owe your lender \$199,439.26 minus \$1251.66. This \$1251.66 represents your 8th month of “forced equity” profit. The 8th month of our loan the \$2415.06 mortgage payment is broken down as follows:

\$ 1163.40- interest to lender (banks profit)

\$ 1251.66- principal payment on loan to reduce debt (our forced equity profit)

By month # 9 you do not owe \$ 199,439.26 any more, you owe \$199,439.26 minus \$1251.66 or \$198,187.60. This is the new principal balance, and since you only pay interest on what you owe your 9th interest payment will be 7 % of \$198,187.60 not \$ 199,439.26. To figure out the 9th month interest we times \$198,187.60 by 7 % equaling \$13,873.13 per year divided by 12 equals \$1156.09 interest owed for the month. This is the profit the bank makes the 9th month on the job. The 8th month we owed the lender

\$1163.40 interest for the month because we owed the lender \$199,439.26, the 9th month we owed the lender **\$ 1156.09** interest for the month (a little less) because the principal balance that we used to calculate the interest owed has been reduced from \$199,439.26 to \$198,187.60. Since the amortized monthly mortgage payment of \$2415.06 doesn't change, its simple subtraction 2415.06 minus **1156.09** equals **1258.97**; this represents the portion of your payment that the lender uses to pay down your debt owed. You now owe your lender \$198,187.60 minus **\$1258.97**. This **\$1258.97** represents your 9th month of "forced equity" profit. The 9th month of our loan the \$2415.06 mortgage payment was broken down as follows:

\$ 1156.09- interest to lender (bank profit)

\$ 1258.97- principal payment on loan to reduce debt (our forced equity profit)

By month # 10 you do not owe \$ 198,187.60 any more, you owe \$198,187.60 minus **\$1258.97** or \$196,928.63. This is the new principal balance, and since you only pay interest on what you owe your 10th month interest payment will be 7 % of \$ 196,928.63 not \$198,187.60. To figure out the 10th month interest we times \$ 196,928.63 by 7 % equaling \$13,785 per year divided by 12 equals **\$ 1148.75** interest owed for the month. This is the profit the bank makes the 10th month on the job. The 9th month we owed the lender **\$1156.09** interest for the month because we owed the lender \$ 198,187.60, the 10th month we owed the lender **\$1148.75** interest for the month (a little less) because the principal balance that we used to calculate the interest owed has been reduced from \$ 198,187.60 to \$196,928.63. Since the amortized monthly mortgage payment of \$2415.06 doesn't change, its simple subtraction 2415.06 minus **\$ 1148.75** equals **\$1266.31**; this represents the portion of your payment that the lender uses to pay down your debt owed. You now owe your lender \$196,928.63 minus **\$1266.31**. This **\$1266.31** represents your 10th month of "forced equity" profit. The 10th month of our loan the \$2415.06 mortgage payment was broken down as follows:

\$ 1148.75- interest to lender (bank profit)

\$ 1266.31- principal payment on loan to reduce debt (our forced equity profit)

By month # 11 you do not owe \$ 196,928.63 any more, you owe \$196,928.63 minus **\$1266.31** or \$195,662.32. This is the new principal balance, and since you only pay interest on what you owe your 11th month interest payment will be 7 % of \$195,662.32 not \$196,928.63. To figure out the 11th month interest we times \$195,662.32 by 7 % equaling \$13,696.36 divided by 12 equals **\$1141.36 interest** owed for the month. This is the profit the bank makes the 11th month on the job. The 10th month we owed the lender **\$1148.75 interest** for the month because we owed the lender \$196,928.63, the 11th month we owed the lender **\$1141.36** interest for the month (a little less) because the principal balance that we used to calculate the interest owed has been reduced from \$196,928.63 to \$195,662.32. Since the amortized monthly mortgage payment of \$2415.06 doesn't change, it's simple subtraction 2415.06 minus **\$1141.36** equals **\$ 1273.70**, this represents the portion of your payment that the lender uses to pay down your debt owed. You now owe your lender \$195,662.32 minus **\$1273.70**. This **\$1273.70** represents your 11th month of "forced equity" profit. The 11th month of our loan the \$2415.06 mortgage payment was broken down as follows:

\$1141.36- interest to lender (bank profit)

\$ 1273.70- principal payment on loan to reduce debt (our forced equity profit)

By month #12 you do not owe \$195, 662.32 any more, you owe \$195,662.32 minus \$1273.70 or \$194,388.62. This is the new principal balance, and since you only pay interest on what you owe your 12th month interest payment will be 7 % of \$194, 388.62 not \$195,662.32. To figure out the 12th month interest we times \$194,388.62 by 7 % equaling \$13,607.20 divided by 12 equals **\$1133.93** interest owed for the month. This is the profit the bank makes the 12th month on the job. The 11th month we owed the lender **\$1141.36** interest for the month because we owed the lender \$195,662.32, the 12th month we owed the lender **\$ 1133.93** interest for the month (a little less) because the principal balance that we used to calculate the interest owed has been reduced from \$195,662.32 to \$194,388.62. Since the amortized monthly mortgage payment of \$2415.06 doesn't change, its simple subtraction 2415.06 minus **\$1133.93** equals **\$1281.13**. This **\$1281.13** represents your 12th month of "forced equity" profit. The 12th and final month of our loan analysis the \$2415.06 mortgage payment was broken down as follows:

\$1133.93- interest to lender (bank profit)

\$1281.13- principal payment on loan to reduce debt (our forced equity profit)

Now lets create a chart, plug our figures in and sum it up. As the chart shows month by month the profit the bank makes gets lower because the principal balance owed that is being used to calculate interest owed is being lowered by the amount of our automatic monthly windfall "forced equity". Month by month our "forced equity" profit gets higher because a larger portion of our pre-determined amortized monthly mortgage payment (2415.06) goes toward reducing the principal balance. The lower the principal balance the lower the interest portion of our amortized mortgage payment.

Look at it this way we pay rent to the lenders (in the form of deductible interest) to use their money and the tenants in turn pay us rent to use the house. The big difference is our rent for using the lenders money is going down month by month and year by year (due to the power of forced equity) and the tenants rent they pay us usually goes up year by year. If the tenant's rent just covered our mortgage payment (principal, interest, property taxes and insurance PITI) and we broke even each month we would still win big because of forced equity. Lets say the tenant paid you \$3000 a month to rent your investment property and your mortgage payment was \$2415.06 and your property taxes were \$6000 a year or \$500 a month and your homeowners insurance was another \$85 per month, on the surface it looks like you are not making any money; you receive \$3000 a month and you pay out \$3000 a month (2415.06 plus 500 plus 85 equals 3000), but now that you are familiar with the concept of amortization and its byproduct "forced equity" you know the truth. After only one year the tenant who invested \$36,000 dollars (\$3000 rent per month for 12 months) has nothing to show for their efforts except a paid bill. On the flip side of the coin, the Landlord who collects the rent and pays the mortgage has plenty to show for their monthly collection effort. If tenant pays one year of rent, the balance owed on the loan is \$193,107.50. (See amortization chart \$208,000 @ 7% 10 yrs). The Landlord just made \$14,892.50 for the year. The old man said you make this \$14,892.50 regardless of whether or not the property went up in value. Translation: If the real estate market stood still- there was no such thing as appreciation; the asset you bought at \$260,000 one year ago was still only worth \$260,000 a year later, you just made \$14,892.50, because you do not owe \$208,000 on the property any more, you only owe \$193,107.50 (\$208,000 original principal balance minus \$14,892.50- scheduled principal payments equals \$193,107.50- new lower principal balance) If the real estate market stood still for another

nine years; now your 10 year mortgage is paid off, and the asset you bought for \$260,000 10 years ago was still only worth \$260,000- you just made \$208,000, because you do not owe \$208,000 on the property any more you owe nothing. The rents that the tenants paid the Landlord over the years have paid the property off through the mechanism of “Forced Equity”. You now have a free and clear asset thanks to your “royal subjects”, your wonderful tenants. The old man looked me square in the eyes and proclaimed “Its good to be the King”.

Amount Financed \$208,000.00
Years 10
Interest Rate 7

Month	Payment	Bank Profit	“Forced Equity” Our Profit	Balance
1	\$2,415.06	\$1,213.33	\$1,201.73	\$206,798.27
2	\$2,415.06	\$1,206.32	\$1,208.74	\$205,589.54
3	\$2,415.06	\$1,199.27	\$1,215.79	\$204,373.75
4	\$2,415.06	\$1,192.18	\$1,222.88	\$203,150.87
5	\$2,415.06	\$1,185.05	\$1,230.01	\$201,920.86
6	\$2,415.06	\$1,177.87	\$1,237.19	\$200,683.67
7	\$2,415.06	\$1,170.65	\$1,244.41	\$199,439.26
8	\$2,415.06	\$1,163.40	\$1,251.66	\$198,187.60
9	\$2,415.06	\$1,156.09	\$1,258.97	\$196,928.63
10	\$2,415.06	\$1,148.75	\$1,266.31	\$195,662.32
11	\$2,415.06	\$1,141.36	\$1,273.70	\$194,388.63
12	\$2,415.06	\$1,133.93	\$1,281.13	\$193,107.50

(\$14,892.50)

The old man said, the best way to learn something is to practice it until it becomes a knee-jerk reaction in your mind; an automatic no thinking involved activity, and then he instructed me to complete the remaining amortization exercises for \$208,000 for 15yrs/20yrs/25yrs and 30yrs. He told me to use the first amortization exercise (\$208,000 @ 7% for 10 years) as a template to figure out how to calculate the 1st year schedule on the four longer-term loans. The old man said, now its your turn to GO FIGURE!!

Amortization Schedule Exercises

You borrow \$208,000 @ 7% interest for 180 months (15yrs)- What is the monthly payment? You go to the chart and find the interest rate first, in this case it is 7.0 and then you find the multiplier per thousand for the term of the loan, in this case 15 years is 8.99 per 1000 dollars borrowed. Now it is simple math $8.99 \times 208 = \$1869.92$.per month. Total payments to lender in 15 years = $\$1869.92 \times 180 \text{ months} = \$336,585.60$. Total profit to bank $\$336,585.60$ minus $\$208,000$ original principal owed = $\$128,585.60$. (****As noted previously the amortization chart per thousand multipliers are estimates only-they are not as exact as the pre programmed computers the lenders use. For your

exercise we will supply the more precise figure. In this example the \$1869.92 payment will be adjusted due to computer accuracy to \$1869.56)

When you have completed your mission this is what your month-by-month chart should look like. After one year your “forced equity” profit is \$8132.34. (\$208,000 original principal balance minus \$199,867.66 new principal balance after scheduled principal loan payments)

Amount Financed	\$208,000.00			
Years	15			
Interest Rate	7			
Monthly Payment	\$1,869.56	Bank Profit	“Forced Equity” Our Profit	
Month	Payment	Interest	Principal	Balance
1	\$1,869.56	\$1,213.33	\$656.23	\$207,343.77
2	\$1,869.56	\$1,209.51	\$660.05	\$206,683.72
3	\$1,869.56	\$1,205.66	\$663.90	\$206,019.81
4	\$1,869.56	\$1,201.78	\$667.78	\$205,352.04
5	\$1,869.56	\$1,197.89	\$671.67	\$204,680.36
6	\$1,869.56	\$1,193.97	\$675.59	\$204,004.77
7	\$1,869.56	\$1,190.03	\$679.53	\$203,325.24
8	\$1,869.56	\$1,186.06	\$683.50	\$202,641.74
9	\$1,869.56	\$1,182.08	\$687.48	\$201,954.26
10	\$1,869.56	\$1,178.07	\$691.49	\$201,262.77
11	\$1,869.56	\$1,174.03	\$695.53	\$200,567.24
12	\$1,869.56	\$1,169.98	\$699.58	\$199,867.66

(8132.34)

You borrow \$208,000 @ 7% interest for 240 months (20yrs)- What is the monthly payment? Once again you go to the chart and find the interest rate first, in this case it is 7.0 and then you find the multiplier per thousand for the term of the loan, in this case 20 years is 7.75 per 1000 dollars borrowed. Now it is simple math $7.75 \times 208 = \$1612$ per month. Total payments to lender in 20 years = $\$1612 \times 240$ months = $\$386,880$. Total profit to bank $\$386,880$ minus $\$208,000$ original principal owed = $\$178,880$. (****In this example the \$1612 amortized monthly mortgage payment will be adjusted due to computer accuracy to \$1612.62)

When you have completed your mission this is what your month-by-month chart should look like. After one year your “forced equity” profit is \$4948.19 (\$208,000 original principal balance minus \$203,051.81 new principal balance after scheduled principal loan payments)

Amount Financed \$208,000.00
Years 20
Interest Rate 7
Monthly Payment \$1,612.62 **Bank Profit** **“Forced Equity” Our Profit**

Month	Payment	Interest	Principal	Balance
1	\$1,612.62	\$1,213.33	\$399.29	\$207,600.71
2	\$1,612.62	\$1,211.00	\$401.62	\$207,199.10
3	\$1,612.62	\$1,208.66	\$403.96	\$206,795.14
4	\$1,612.62	\$1,206.30	\$406.32	\$206,388.82
5	\$1,612.62	\$1,203.93	\$408.69	\$205,980.14
6	\$1,612.62	\$1,201.55	\$411.07	\$205,569.07
7	\$1,612.62	\$1,199.15	\$413.47	\$205,155.60
8	\$1,612.62	\$1,196.74	\$415.88	\$204,739.72
9	\$1,612.62	\$1,194.32	\$418.30	\$204,321.42
10	\$1,612.62	\$1,191.87	\$420.75	\$203,900.67
11	\$1,612.62	\$1,189.42	\$423.20	\$203,477.47
12	\$1,612.62	\$1,186.95	\$425.67	\$203,051.81

(\$4948.19)

You borrow \$208,000 @7% interest for 300 months (25 yrs)- What is the monthly payment ? You go to the chart and find the interest rate first, in this case it is 7.0 and then you find the multiplier per thousand for the term of the loan, in this case 25 years is 7.07 per 1000 dollars borrowed. Now it is simple math $7.07 \times 208 = \$1470.56$ per month. Total payments to lender in 25 years = $\$1470.56 \times 300$ months = $\$441,168$. Total profit to bank $\$441,168$ minus $\$208,000$ original principal owed = $\$233,168$.
 (**** In this example the $\$1470.56$ amortized monthly mortgage payment will be adjusted due to computer accuracy to $\$1470.10$.

When you have completed your mission this is what your month-by-month chart should look like. After one year your “forced equity” profit is $\$3182$ ($\$208,000$ original principal balance minus $\$204,818$ new principal balance after scheduled principal loan payments)

Amount Financed \$208,000.00
Years 25
Interest Rate 7
Monthly Payment \$1,470.10 **Bank Profit** **“Forced Equity” Our Profit**

Month	Payment	Interest	Principal	Balance
1	\$1,470.10	\$1,213.33	\$256.77	\$207,743.23
2	\$1,470.10	\$1,211.84	\$258.26	\$207,484.97

3	\$1,470.10	\$1,210.33	\$259.77	\$207,225.20
4	\$1,470.10	\$1,208.81	\$261.29	\$206,963.91
5	\$1,470.10	\$1,207.29	\$262.81	\$206,701.10
6	\$1,470.10	\$1,205.76	\$264.34	\$206,436.76
7	\$1,470.10	\$1,204.21	\$265.89	\$206,170.87
8	\$1,470.10	\$1,202.66	\$267.44	\$205,903.44
9	\$1,470.10	\$1,201.10	\$269.00	\$205,634.44
10	\$1,470.10	\$1,199.53	\$270.57	\$205,363.87
11	\$1,470.10	\$1,197.96	\$272.14	\$205,091.73
12	\$1,470.10	\$1,196.37	\$273.73	\$204,818.00

(\$3182)

The final analysis will be \$208,000 @ 7 % for 360 months (30yrs). What is the monthly payment? You should know the routine by now, you go to the chart and find the interest rate first, in this case it is 7.0 and then you find the multiplier per thousand for the term of the loan, in this case 30 years is 6.65 per 1000 dollars borrowed. Now it is simple math $6.65 \times 208 = \$1383.20$ per month. Total payments to lender in 30 years = $\$1383.20 \times 360$ months = \$497,952. Total profit to bank \$497,952 minus \$208,000 original principal owed = \$289,952.

(****In this example the \$1383.20 amortized monthly mortgage payment will be adjusted due to computer accuracy to \$1383.83)

When you have completed this final mission this is what your month-by-month chart should look like. After one year your “forced equity” profit is \$2112.89. (\$208,000 original principal balance minus \$205,887.11 new principal balance after scheduled principal loan payments)

Amount				
Financed	\$208,000.00			
Years	30			
Interest				
Rate	7			
Monthly				
Payment	\$1,383.83	Bank Profit	“Forced Equity”	
			Our Profit	
Month	Payment	Interest	Principal	Balance
1	\$1,383.83	\$1,213.33	\$170.50	\$207,829.50
2	\$1,383.83	\$1,212.34	\$171.49	\$207,658.01
3	\$1,383.83	\$1,211.34	\$172.49	\$207,485.52
4	\$1,383.83	\$1,210.33	\$173.50	\$207,312.02
5	\$1,383.83	\$1,209.32	\$174.51	\$207,137.51
6	\$1,383.83	\$1,208.30	\$175.53	\$206,961.99
7	\$1,383.83	\$1,207.28	\$176.55	\$206,785.43

8	\$1,383.83	\$1,206.25	\$177.58	\$206,607.85
9	\$1,383.83	\$1,205.21	\$178.62	\$206,429.23
10	\$1,383.83	\$1,204.17	\$179.66	\$206,249.57
11	\$1,383.83	\$1,203.12	\$180.71	\$206,068.87
12	\$1,383.83	\$1,202.07	\$181.76	\$205,887.11

(\$2112.89)

After successfully completing these 4 amortization missions, you should be a master at this concept, if not go back to the exercises and practice some more until you are. The old man said real estate investing is a simple business “the more you learn, the more you earn” and you need to be an expert at amortization and the concept of forced equity in order to realize your maximum profit as a real estate investor.

The” numbers don’t lie “ the old man said, the longer you owe the money the more money the vulture bankers make off of you. If you sacrifice and scrimp and scrounge and go for the shorter 15 year fully amortized loan payment of \$1869.92 instead of the more affordable 30 year fully amortized loan payment of \$1383.20 you pay \$128,585.60 in interest to lender instead of \$289,952 in interest a savings of \$161, 366.40. You legally get to beat the bank out of over \$161,000 dollars in profit just by making the simple decision of adjusting the payback timetable from 30 yrs to 15 yrs. The old man said, “interest is tabulated based on principal balance reduction,” so the quicker you reduce your debt owed to the lender the more money you save. There are essentially two ways to defeat the banks money making interest machine a) reduce principal balance owed quicker by raising your mortgage payment and amortizing loan over a shorter period of time (in our case \$208k @ 7% 30 yr = \$1383.20 versus \$208k @7% 15 yr= \$1869.92 a \$486.72 per month difference) and b) keep the mortgage payment low by amortizing loan over longer period of time (keep the affordable 30 yr payment \$ 1383.20) and make unscheduled principal payments on loan thereby reducing interest owed and shortening time required to payback monies. The old man said there is a third way to defeat the banks at their own game, make enough money from your investments to pay no interest by paying all cash for your home, but since most people are not in that position, learning the ins and outs of the mortgage process and borrowing the money makes the most sense .I asked the old man what do you do if you really can’t afford the higher payment now but maybe in the future you might be able to swing it, do you refinance the loan from the 30 year down to the 15 year ? Absolutely not, you should save the money you would have spent on closing costs and make unscheduled principal payments instead. You would be surprised what a one time \$5000 unscheduled principal payment on a \$208,000 loan @7% 30 yr actually does. Lets do the calculations and see.

Before you get started you will need a *reference tool*; the month-by-month amortization schedule for \$208,000 @ 7 % for 30 years. (For illustration purposes we will show first 10yrs of schedule)

Unscheduled Principal Payments:

- Save money- less interest paid
- Save time- less years to pay back
- Lowers effective rate of interest

- Truth of the bi-weekly mortgage

REFERENCE TOOL - 10 yrs of 30 yr Amortization Schedule \$208,000 @ 7 %

Home Price \$260,000.00
Down Payment \$52,000.00
Amount Financed \$208,000.00
Years 30
Interest Rate 7
Monthly Payment \$1,383.83

Month	Payment	Interest	Principal	Balance
1	\$1,383.83	\$1,213.33	\$170.50	\$207,829.50
2	\$1,383.83	\$1,212.34	\$171.49	\$207,658.01
3	\$1,383.83	\$1,211.34	\$172.49	\$207,485.52
4	\$1,383.83	\$1,210.33	\$173.50	\$207,312.02
5	\$1,383.83	\$1,209.32	\$174.51	\$207,137.51
6	\$1,383.83	\$1,208.30	\$175.53	\$206,961.99
7	\$1,383.83	\$1,207.28	\$176.55	\$206,785.43
8	\$1,383.83	\$1,206.25	\$177.58	\$206,607.85
9	\$1,383.83	\$1,205.21	\$178.62	\$206,429.23
10	\$1,383.83	\$1,204.17	\$179.66	\$206,249.57
11	\$1,383.83	\$1,203.12	\$180.71	\$206,068.87
12	\$1,383.83	\$1,202.07	\$181.76	\$205,887.11
13	\$1,383.83	\$1,201.01	\$182.82	\$205,704.28
14	\$1,383.83	\$1,199.94	\$183.89	\$205,520.40
15	\$1,383.83	\$1,198.87	\$184.96	\$205,335.43
16	\$1,383.83	\$1,197.79	\$186.04	\$205,149.39
17	\$1,383.83	\$1,196.70	\$187.13	\$204,962.27
18	\$1,383.83	\$1,195.61	\$188.22	\$204,774.05
19	\$1,383.83	\$1,194.52	\$189.31	\$204,584.74
20	\$1,383.83	\$1,193.41	\$190.42	\$204,394.32
21	\$1,383.83	\$1,192.30	\$191.53	\$204,202.79
22	\$1,383.83	\$1,191.18	\$192.65	\$204,010.14
23	\$1,383.83	\$1,190.06	\$193.77	\$203,816.37
24	\$1,383.83	\$1,188.93	\$194.90	\$203,621.47
25	\$1,383.83	\$1,187.79	\$196.04	\$203,425.43
26	\$1,383.83	\$1,186.65	\$197.18	\$203,228.25
27	\$1,383.83	\$1,185.50	\$198.33	\$203,029.92
28	\$1,383.83	\$1,184.34	\$199.49	\$202,830.43
29	\$1,383.83	\$1,183.18	\$200.65	\$202,629.78
30	\$1,383.83	\$1,182.01	\$201.82	\$202,427.95
31	\$1,383.83	\$1,180.83	\$203.00	\$202,224.95
32	\$1,383.83	\$1,179.65	\$204.18	\$202,020.77
33	\$1,383.83	\$1,178.45	\$205.38	\$201,815.39
34	\$1,383.83	\$1,177.26	\$206.57	\$201,608.82
35	\$1,383.83	\$1,176.05	\$207.78	\$201,401.04
36	\$1,383.83	\$1,174.84	\$208.99	\$201,192.05
37	\$1,383.83	\$1,173.62	\$210.21	\$200,981.84

Tim Larkin
King of the Middle Cass
www.rkcnys.com

38	\$1,383.83	\$1,172.39	\$211.44	\$200,770.41
39	\$1,383.83	\$1,171.16	\$212.67	\$200,557.74
40	\$1,383.83	\$1,169.92	\$213.91	\$200,343.83
41	\$1,383.83	\$1,168.67	\$215.16	\$200,128.67
42	\$1,383.83	\$1,167.42	\$216.41	\$199,912.26
43	\$1,383.83	\$1,166.15	\$217.68	\$199,694.58
44	\$1,383.83	\$1,164.89	\$218.94	\$199,475.64
45	\$1,383.83	\$1,163.61	\$220.22	\$199,255.41
46	\$1,383.83	\$1,162.32	\$221.51	\$199,033.91
47	\$1,383.83	\$1,161.03	\$222.80	\$198,811.11
48	\$1,383.83	\$1,159.73	\$224.10	\$198,587.01
49	\$1,383.83	\$1,158.42	\$225.41	\$198,361.60
50	\$1,383.83	\$1,157.11	\$226.72	\$198,134.88
51	\$1,383.83	\$1,155.79	\$228.04	\$197,906.84
52	\$1,383.83	\$1,154.46	\$229.37	\$197,677.47
53	\$1,383.83	\$1,153.12	\$230.71	\$197,446.75
54	\$1,383.83	\$1,151.77	\$232.06	\$197,214.70
55	\$1,383.83	\$1,150.42	\$233.41	\$196,981.29
56	\$1,383.83	\$1,149.06	\$234.77	\$196,746.51
57	\$1,383.83	\$1,147.69	\$236.14	\$196,510.37
58	\$1,383.83	\$1,146.31	\$237.52	\$196,272.85
59	\$1,383.83	\$1,144.92	\$238.91	\$196,033.95
60	\$1,383.83	\$1,143.53	\$240.30	\$195,793.65
61	\$1,383.83	\$1,142.13	\$241.70	\$195,551.95
62	\$1,383.83	\$1,140.72	\$243.11	\$195,308.84
63	\$1,383.83	\$1,139.30	\$244.53	\$195,064.31
64	\$1,383.83	\$1,137.88	\$245.95	\$194,818.35
65	\$1,383.83	\$1,136.44	\$247.39	\$194,570.97
66	\$1,383.83	\$1,135.00	\$248.83	\$194,322.13
67	\$1,383.83	\$1,133.55	\$250.28	\$194,071.85
68	\$1,383.83	\$1,132.09	\$251.74	\$193,820.10
69	\$1,383.83	\$1,130.62	\$253.21	\$193,566.89
70	\$1,383.83	\$1,129.14	\$254.69	\$193,312.20
71	\$1,383.83	\$1,127.65	\$256.18	\$193,056.03
72	\$1,383.83	\$1,126.16	\$257.67	\$192,798.36
73	\$1,383.83	\$1,124.66	\$259.17	\$192,539.18
74	\$1,383.83	\$1,123.15	\$260.68	\$192,278.50
75	\$1,383.83	\$1,121.62	\$262.21	\$192,016.29
76	\$1,383.83	\$1,120.10	\$263.73	\$191,752.56
77	\$1,383.83	\$1,118.56	\$265.27	\$191,487.28
78	\$1,383.83	\$1,117.01	\$266.82	\$191,220.46
79	\$1,383.83	\$1,115.45	\$268.38	\$190,952.09
80	\$1,383.83	\$1,113.89	\$269.94	\$190,682.14
81	\$1,383.83	\$1,112.31	\$271.52	\$190,410.63
82	\$1,383.83	\$1,110.73	\$273.10	\$190,137.53
83	\$1,383.83	\$1,109.14	\$274.69	\$189,862.83
84	\$1,383.83	\$1,107.53	\$276.30	\$189,586.53
85	\$1,383.83	\$1,105.92	\$277.91	\$189,308.63
86	\$1,383.83	\$1,104.30	\$279.53	\$189,029.10
87	\$1,383.83	\$1,102.67	\$281.16	\$188,747.94
88	\$1,383.83	\$1,101.03	\$282.80	\$188,465.13
89	\$1,383.83	\$1,099.38	\$284.45	\$188,180.68

Tim Larkin
King of the Middle Cass
www.rkrynys.com

90	\$1,383.83	\$1,097.72	\$286.11	\$187,894.58
91	\$1,383.83	\$1,096.05	\$287.78	\$187,606.80
92	\$1,383.83	\$1,094.37	\$289.46	\$187,317.34
93	\$1,383.83	\$1,092.68	\$291.15	\$187,026.19
94	\$1,383.83	\$1,090.99	\$292.84	\$186,733.35
95	\$1,383.83	\$1,089.28	\$294.55	\$186,438.80
96	\$1,383.83	\$1,087.56	\$296.27	\$186,142.53
97	\$1,383.83	\$1,085.83	\$298.00	\$185,844.53
98	\$1,383.83	\$1,084.09	\$299.74	\$185,544.79
99	\$1,383.83	\$1,082.34	\$301.49	\$185,243.31
100	\$1,383.83	\$1,080.59	\$303.24	\$184,940.06
101	\$1,383.83	\$1,078.82	\$305.01	\$184,635.05
102	\$1,383.83	\$1,077.04	\$306.79	\$184,328.26
103	\$1,383.83	\$1,075.25	\$308.58	\$184,019.68
104	\$1,383.83	\$1,073.45	\$310.38	\$183,709.29
105	\$1,383.83	\$1,071.64	\$312.19	\$183,397.10
106	\$1,383.83	\$1,069.82	\$314.01	\$183,083.09
107	\$1,383.83	\$1,067.98	\$315.85	\$182,767.24
108	\$1,383.83	\$1,066.14	\$317.69	\$182,449.56
109	\$1,383.83	\$1,064.29	\$319.54	\$182,130.01
110	\$1,383.83	\$1,062.43	\$321.40	\$181,808.61
111	\$1,383.83	\$1,060.55	\$323.28	\$181,485.33
112	\$1,383.83	\$1,058.66	\$325.17	\$181,160.16
113	\$1,383.83	\$1,056.77	\$327.06	\$180,833.10
114	\$1,383.83	\$1,054.86	\$328.97	\$180,504.13
115	\$1,383.83	\$1,052.94	\$330.89	\$180,173.24
116	\$1,383.83	\$1,051.01	\$332.82	\$179,840.42
117	\$1,383.83	\$1,049.07	\$334.76	\$179,505.66
118	\$1,383.83	\$1,047.12	\$336.71	\$179,168.95
119	\$1,383.83	\$1,045.15	\$338.68	\$178,830.27
120	\$1,383.83	\$1,043.18	\$340.65	\$178,489.62

In a traditional mortgage loan of \$208,000 @ 7 % interest for 30 years, we would have 360 equal payments of \$1383.83. That’s \$1383.83 times 360 equals \$498,178.80 total payments to lender. If we subtract the original principal balance that we borrowed \$208,000 from the total payment of \$498,178.80 we get \$290,178.80; the banks profit; the interest that we paid over a 30 year period of time to borrow this money at a 7 % annual yield to lender. In a traditional ‘meat and potatoes loan “ with no unscheduled principal payments we would pay our lender a whopping \$290,178.80 profit.

Most traditional mortgage loans have a standard one year pre payment penalty clause (usually 5% of unpaid principal balance) in the mortgage documents if you pay any or all of the loan off in the first 12 months, so in order to avoid incurring this fee (in our case 5% of \$208,000 or \$10,400) it is beneficial to wait a year or so before you embark on your money saving, time saving unscheduled principal payment investment strategy. The first 12 months of the loan you

will pay the same interest as a traditional “meat and potatoes “ loan; \$14,493.06 (add up all 12 columns).

Amount Financed	\$208,000.00			
Years	30			
Interest Rate	7			
Monthly Payment	\$1,383.83	Bank Profit	“Forced Equity” Our Profit	
Month	Payment	Interest	Principal	Balance
1	\$1,383.83	\$1,213.33	\$170.50	\$207,829.50
2	\$1,383.83	\$1,212.34	\$171.49	\$207,658.01
3	\$1,383.83	\$1,211.34	\$172.49	\$207,485.52
4	\$1,383.83	\$1,210.33	\$173.50	\$207,312.02
5	\$1,383.83	\$1,209.32	\$174.51	\$207,137.51
6	\$1,383.83	\$1,208.30	\$175.53	\$206,961.99
7	\$1,383.83	\$1,207.28	\$176.55	\$206,785.43
8	\$1,383.83	\$1,206.25	\$177.58	\$206,607.85
9	\$1,383.83	\$1,205.21	\$178.62	\$206,429.23
10	\$1,383.83	\$1,204.17	\$179.66	\$206,249.57
11	\$1,383.83	\$1,203.12	\$180.71	\$206,068.87
12	\$1,383.83	\$1,202.07	\$181.76	\$205,887.11

(\$14,493.06)

After 12 months the principal balance remaining on loan is \$205,887.11. If on the 13th month you made an unscheduled principal payment (a pre-payment) to the lender in the amount of \$5000 you would have to consult the reference tool ;(the amortization table for \$208,000 @7 % for 30 yrs) to figure out how much interest you saved and how much time you chopped off your loan.

The \$5000 unscheduled principal payment comes directly off the principal balance remaining on the loan, none of this money is profit to the bank, it is all used to reduce the balance owed. (This is not costing you any extra money, you rightfully owe this money anyway, you are just giving them a portion of their money a little earlier than expected, and in return you are accelerating the payback schedule and saving the interest you would have paid had you kept their money longer) The payment of \$1383.83 remains the same, but the amount of overall interest that we pay and time that we have to pay it has changed substantially.

By month # 13 we do not owe \$205,887.11 any more, we owe \$205,887.11 minus \$5,000 or \$200,887.11. Now we have to consult our reference tool (pg # 16) and find out which month of our loan schedule comes closes to our new principal balance of \$200,887.11. We find our answer at month # 37. The principal balance remaining after 37 months of scheduled mortgage payments is \$200,981.84. If we paid our loan as per our old schedule of payments we would have owed our bank their profit from month #13 thru month #36, but the pre-pay jumps us over these 24

payments and places us in the 37th amortized payment position. In essence our 13th payment becomes our 37th payment in our schedule. It would have taken us an extra 2 years of normal principal payments (green column) to get to the same point in our amortization schedule that one lump sum of \$5000 does in one day. This unscheduled principal payment has moved us from month #13 to month # 37, chopping off 2 years of mortgage payments and saving the interest we would have owed from month # 13 to month # 37(add up all red columns for those months) or \$28,516.87.

You now have a loan with the same monthly payment of \$1383.83 but you only have 27 years remaining not 29. The bank is not making the full \$290, 178.80 that a 7 % yield would have given them had you kept to the original schedule of payments; the bank is making \$290,178.80 minus \$28, 516.87 or \$261,661.93. The pre payment actually lowers the profit the bank makes, effectively lowering the rate of interest that you were charged for renting this money. I looked at my old man incredulously, and said you mean I don't have to refinance to lower my rate of interest; I can just make unscheduled principal payments and accomplish the same thing? The old man said absolutely, now lets prove it. In our example the bank would have to make \$290, 178.80 profit over a 30 year period to make an annual 7 % profit, so obviously if our bank made only \$261,661.93 in profit over the same 30 year period the annual % has to be lower. The question you have to solve is what effective rate of interest would generate a profit of \$261,661.93 on a loan amount of \$208,000? The easiest way to do it is to go to your computer and plug different interest rate variables in until you get to the one closest to the profit generated. In our case that would be 6.426 %. The first year of the loan you would pay the same 7 % yield to the bank; the moment you pre pay your meat & potato loan, you change the effective yield of the loan from that point on. In our case we paid 7 % the first year and 6.426 % for subsequent years. If we made a \$5000 unscheduled pre-pay after say 10 years; the first 10 years of the loan we would pay a 7 % yield to the bank, and then we would pay a 6.426 % effective rate of interest on any remaining payments to lender. (Years 1-10 you paid 7 %, years 11,12,13,14 and so on you are effectively paying a rate of 6.426 %, If you were to make more unscheduled principal payments you would reduce the effective rate of interest even lower, because you would legally beat the lender out of more of it's profit)

Without Pre- Pay

“Meat & Potato Fixed rate loan “

With Pre-Pay

“Meat & Potato fixed rate loan w/ gravy”

Home Price -	\$260,000	Home Price -	\$260,000
Down Payment -	\$ 52,000 (20%)	Down Payment -	\$ 52,000 (20%)
% Rate	7%	% Rate	6.426%
Period (Years) 30		Period (Years) 30	
Amount Financed -	\$208,000	Amount Financed -	\$208,000
Total Number of Payments -	360	Total Number of Payments -	360
Total Payments -	\$498,178.51	Total Payment -	\$469,654.31
Total Interest Payments	\$290,178.51	Total Interest Payments	\$261,654.31

Translation: By making a one time unscheduled \$5000 principal payment on our loan we have saved over twenty eight thousand dollars in interest, shaved almost 2 years off of our scheduled payments and lowered the effective interest rate that we were initially charged to borrow the money from 7 % to approximately 6.426 %. The old man called this pre- payment investing strategy the *gravy* on the standard “meat & potato fixed rate” loan. The money and time you save by employing this tactic makes the loan much more palatable.

I asked the old man; if I don’t have the extra \$5000 lying around can’t I accomplish the same thing by just calling up those companies that arrange bi-weekly mortgages. ? You know, keep the same mortgage payment but pay every 2 weeks instead of once a month. The old man responded, the bi weekly mortgage is nothing more than a masqueraded unscheduled principal payment, basically its 13 payments a year not 12. The numbers don’t lie son, Do the Math!! Use our loan as an **Example;**

\$208,000 @ 7% 30 years= \$1383.83 per month for 12 months = \$16,605.96 for year.

Add one extra unscheduled principal payment (13th payment): \$1383.83 for year

Total monies tendered to bank for the year: \$17,989.79

**Bi-weekly: Take the \$1383.83 per month divide it by 2 = \$691.92 every 2 weeks
(There are 52 weeks in a year, so we will pay this \$691.92 for 26 weeks)**

\$208,000 @ 7 % 30 years = \$691.92 X 26 weeks = \$17,989.92

Total monies tendered to bank for the year: \$17,989.92

As the numbers clearly show there is no monetary difference between a bi weekly mortgage product and an unscheduled principal payment. Both options require the same expenditure \$17,989 give or take the cents. Basically with a bi weekly mortgage you are making an unscheduled principal payment of one full monthly mortgage payment per year. In our case you are making an unscheduled principal payment of \$ 1383.83 per year minus the fees these companies may charge for their service. (Typical fees: one time setup fee of about \$200-\$500, plus a service fee of \$2.50 to \$4.50 for each biweekly payment. A typical 30-year loan can be wiped out in approximately 22 years and you would wind up paying \$1600 -\$2000 in fees)

The old man said “why pay thousands when you can do it yourself? “ It’s easy, no specialized software or fancy accounting needed. All you are really doing with a bi weekly mortgage is paying someone else \$1600-\$2000 for knowledge of something I have just taught you, and you should know by now, namely the money saving, time saving knowledge of how “forced equity” works .Its easy, all you have to do is save up some extra money; make an unscheduled principal payment and use your amortization schedule (your reference tool for this investing strategy) to keep your lender honest and to verify with exact figures how much interest you saved and years you chopped off your loan and bingo you eliminate the services of a middle man by doing it yourself. The old man said instead of wasting your hard earned dollars on this bogus service you would be better served investing that same \$1600-\$2000 as your first unscheduled principal payment. As I showed previously a one time \$5000 pre pay nets you over \$28,000 in savings, you can and should do the calculations for how much a \$1600 or \$2000 pre pay would net you before you invest; you wouldn’t be able to justify the expense otherwise. You should also figure out how much time & interest you save by making that extra unscheduled 13th payment of \$1383.83 every year.

I asked the old man, “if I don’t have any extra money to invest in unscheduled principal payments shouldn’t I lower my mortgage payments each month by getting involved with the ever

popular interest only mortgage loan? The old man gave me a quizzical look and stated interest only loans are not a separate type of mortgage, interest only is an *option* that can be attached to any type of mortgage loan. Basically you chose not to a) employ the powerful concept of amortization & forced equity (that you just learned) and b) pay any principal payments per month on loan. The monthly payment is for interest only. Using our reference tool as a guide (amortization schedule -\$208,000 @ 7% 30 yrs) we can clearly show the difference between the standard “meat & potato fixed rate loan” and the interest only *option*. In the case of an *interest-only-loan* the monthly payments would be \$1,213.33 versus \$1,383.83, which would “save” you \$170 per month in the short term, but in the long term you would loose the *power of forced equity* By going for the small buck you lose out on the big buck.

“Meat & Potato fixed rate amortized loan payment- \$1383.83”

Amount				
Financed \$208,000.00				
Years 30				
Interest				
Rate 7				
Monthly Payment \$1,383.83		Bank Profit	“Forced Equity” Our Profit	
Month	Payment	Interest	Principal	Balance
1	\$1,383.83	\$1,213.33	\$170.50	\$207,829.50
2	\$1,383.83	\$1,212.34	\$171.49	\$207,658.01
3	\$1,383.83	\$1,211.34	\$172.49	\$207,485.52
4	\$1,383.83	\$1,210.33	\$173.50	\$207,312.02
5	\$1,383.83	\$1,209.32	\$174.51	\$207,137.51
6	\$1,383.83	\$1,208.30	\$175.53	\$206,961.99
7	\$1,383.83	\$1,207.28	\$176.55	\$206,785.43
8	\$1,383.83	\$1,206.25	\$177.58	\$206,607.85
9	\$1,383.83	\$1,205.21	\$178.62	\$206,429.23
10	\$1,383.83	\$1,204.17	\$179.66	\$206,249.57
11	\$1,383.83	\$1,203.12	\$180.71	\$206,068.87
12	\$1,383.83	\$1,202.07	\$181.76	\$205,887.11

“Interest only Non-amortized loan payment - \$1213.33”

Amount Financed	\$208,000.00			
Years	30			
Interest Rate	7			
Monthly Payment	\$1213.33	Bank Profit	“Forced Equity” Our Profit	

Month	Payment	Interest	Principal	Balance
1	\$1,213.33	\$1,213.33	0	\$208,000.00
2	\$1,213.33	\$1,213.33	0	\$208,000.00
3	\$1,213.33	\$1,213.33	0	\$208,000.00
4	\$1,213.33	\$1,213.33	0	\$208,000.00
5	\$1,213.33	\$1,213.33	0	\$208,000.00
6	\$1,213.33	\$1,213.33	0	\$208,000.00
7	\$1,213.33	\$1,213.33	0	\$208,000.00
8	\$1,213.33	\$1,213.33	0	\$208,000.00
9	\$1,213.33	\$1,213.33	0	\$208,000.00
10	\$1,213.33	\$1,213.33	0	\$208,000.00
11	\$1,213.33	\$1,213.33	0	\$208,000.00
12	\$1,213.33	\$1,213.33	0	\$208,000.00

The logic of the bankers hawking these interest only loans to investors is as follows:
 The interest only loan has a lower monthly payment than the standard amortized loan and therefore the investor’s positive cash flow (the money the investor has left in his pocket after the tenant pays all his bills on the rental property) is higher. If the investor had a tenant paying say \$2000 a month and the standard amortized loan repayment was \$1383.83 the investor would gross \$616.17 a month. If the same investor had an interest only loan the repayment would be \$1213.33 a month and the investor would gross \$786.67 a month. Lets see, do I the investor want to pocket \$786 a month or \$616 a month to borrow the same amount of money? It seems on the surface that the banker is being uncharacteristically kind to the investor; like the money the banker is lending you is on sale. In the above example the investor would safely assume since her payments are \$170 dollars per month less that she was in a better position with this loan than the standard meat and potato-amortized loan. The thing is the bankers do not really care about the investor’s bottom-line, they are in the business of peddling loans and making money by renting out money. The more people they can qualify to rent their money the more profits they realize. The real logic of the bankers pushing these loans is simple: the interest only loan is a

lower payment than the standard amortized loan and will allow the bankers to lend the investor more money and therefore the bankers make more money. The bankers are not concerned about the investor's bottom-line; they are concerned about their own bottom-line. Let's not take my word for it – let's do the homework. Let's crunch the numbers. **The Numbers Don't Lie.** Let's compare apples to apples. Let's make believe **Investor A** bought a rental for \$260,000 with a 20% down payment (\$52,000) and financed the balance of the purchase price with a \$208,000 interest-only loan. **Investor B** bought a similar rental for \$260,000 with a 20% down payment (\$52,000) and financed the balance owed with a standard meat and potato, no-frills amortized loan of \$208,000. Let's go ten years into the future and see how each investor did.

Investor A spent \$145,599.60 in mortgage payments versus \$166,059.60 for investor B. On the surface it looks like investor A was the big winner because they spent \$20,460 less than investor B (\$166,059.60 - \$145,599.60). But investor B has a bonus plan attached to its payments, almost like a rebate program, it's called Forced Equity and for the \$166,059.60 spent on mortgage payments this investor gets back \$29,510.38 meaning they only spent \$136,549.22, \$9,050.38 less (\$145,599.60 - \$136,549.22) than investor A. After 10 years Investor B is ahead by \$9,050.38 and growing. Each month the mortgage payment is made investor B, with the power of forced equity, is pulling further and further ahead of Investor A. Furthermore Investor A has a poison pill attached to its loan, it's called the balloon payment. A balloon payment is the agreed-upon time that the lender wants the investor (5, 10, 15 years), who was only paying interest on the loan, to pay back the entire principal balance owed on the loan (the balloon payment is due & payable) which means the investor must refinance the house and incur at least \$10,400 (5%) in closing costs to do so. Translation: if you have a \$208,000 interest-only loan that is due and payable in full in 10 years, you will owe \$208,000 in 10 years because you chose not to make any principal payments, it was your *option*. You will be forced to waste money on a refi or bail out of the investment and sell the house to pay the lender back. That means investor B is now ahead \$9,050.38 plus \$10,400 for a grand 10-year total of \$19,450.38.

\$208,000 @ 7% Interest only Option versus Self Amortizing
FINANCIAL COMPARISON

<u>Investor A</u> <u>INTEREST ONLY</u>	<u>Investor B</u> <u>SELF AMORTIZING</u>	<u>Investor B bonus</u> <u>FORCED EQUITY*</u>
<u>Year 1:</u> 1,213.33 x 12 = 14,559.96 for the year	<u>Year 1:</u> 1,383.83 x 12 = 16,605.96 for the year	\$208,000.00 - \$205,887.11 = \$2,112.89
<u>Year 2:</u> 1,213.33 x 12 = 14,559.96 for the year	<u>Year 2:</u> 1,383.83 x 12 = 16,605.96 For the year	\$205,887.11 - \$203,621.47 = \$2,265.64
<u>Year 3:</u> 1,2113.33 x 12 = 14,559.96 for the year	<u>Year 3:</u> 1,383.83 x 12 = 16,605.96 for the year	\$203,621.47 - \$201,192.05 = \$2,429.42
<u>Year 4:</u> 1,2113.33 x 12 = 14,559.96 for the year	<u>Year 4:</u> 1,383.83 x 12 = 16,605.96 for the year	\$201,192.05 - \$198,587.01 = \$2,605.04
<u>Year 5:</u> 1,2113.33 x 12 = 14,559.96 for the year	<u>Year 5:</u> 1,383.83 x 12 = 16,605.96 for the year	\$198,587.01 - \$195,793.65 = \$2,793.36

Tim Larkin
King of the Middle Cass
www.rkcnys.com

<u>Year 6:</u> 1,2113.33 x 12 = 14,559.96 for the year	<u>Year 6:</u> 1,383.83 x 12 = 16,605.96 for the year	\$195,793.65-\$192,798.36=\$2995.29
<u>Year 7:</u> 1,2113.33 x 12 = 14,559.96 for the year	<u>Year 7:</u> 1,383.83 x 12 = 16,605.96 for the year	\$192,798.36-\$189,586.53=\$3211.83
<u>Year 8:</u> 1,2113.33 x 12 = 14,559.96 for the year	<u>Year 8:</u> 1,383.83 x 12 = 16,605.96 for the year	\$189,586.53-\$186,142.53=\$3444
<u>Year 9:</u> 1,2113.33 x 12 = 14,559.96 for the year	<u>Year 9:</u> 1,383.83 x 12 = 16,605.96 for the year	\$186,142.53-\$182,449.56=\$3692.97
<u>Year 10:</u> 1,2113.33 x 12 = 14,559.96 for the year Balance owed after 10 years \$208,000 Balloon Payment due- (*Poison Pill *) \$208,000- 2 choices 1) Refinance and pay off balloon . cost estimate 5%- of \$208,000= 10,400 2) Forced to sell	<u>Year 10:</u> 1,383.83 x 12 = 16,605.96 for the year	\$182,449.56-\$178,489.62=\$3692.97 Balance owed after 10 years= \$178,489.62
Total money spent in 10 Years= 14,559.96 x 10 = \$145,599.60 plus \$10,400 to pay off balloon= \$155,999.60	Total money spent in 10 Years = 16,605.96 x 10= \$166,059.60	Landlord Rebate Program – Forced monthly equity. (120 months) \$208,000-\$178,489.62= \$29,510.38

* Forced equity is a by product of self amortizing loan

* Refer to Reference tool - amortization schedule 208,000 @ 7 % 30 years

Total Money spent in 10 years:

Investor A-\$155,999.60

Investor B- \$136,549.22

Investor B is \$19,450.38 richer because of the concept of forced equity. In 20 more years Investor B will have an asset paid for in full by using tenants rent money coupled with the powerful investing mechanism of Forced Equity.

An investor should

Never Ever take out an interest only loan unless:

1. FLIPS-Short term hold position (3months –1 year)- Buy low, fix up sell high. Interest only loan keeps holding costs down. (Remember our example- 1213.33 versus 1383.83) While the investor is waiting to resell the property at a profit the expenses are lower. Less holding costs = more profit

OR

2. Appreciation only investing in red hot sellers market- The interest only loan keeps holding costs down while the forces of the market drive the price up and the investor unloads the property at a tidy profit – usually within 3-5 years.(RISKY- this investor only wins if real estate market is going up- if real estate market is stagnant or in a down spiral- investor could be forced to sell at a loss- These investors are equivalent to speculators- they are short term opportunists- They do not enjoy the protection of forced equity that the long term investors have built into their system of investing.)

OR

3. Long term investing for the Disciplined Saver- a disciplined saver can win big with an interest only loan. They can increase their Positive cash flow month-by-month or semiannually by making unscheduled principal payments on loan. The investor can pre pay this loan from day one, unlike the meat & potato amortized loan that usually has a one-year pre payment penalty attached to it. Remember these payments will actually lower the overall monthly mortgage payment per month. The one big advantage of a non-amortized loan is that the payment per month actually goes down when you make an unscheduled principal payment unlike the meat & potato amortized loan where the payment stays constant but the time to repay the loan decreases.

In an interest only loan if you owed say \$208,000 @ 7% your interest only payment would be \$1213.33, (208,000 times 7 % = 14,560 divided by 12 = 1213.33) but if you gave the lender a 10,000 payment towards principal you would owe 208,000 minus 10,000 or 198,000. Your new payment would be 198,000 times 7 %, which is \$13,860 per year divided by 12 would be 1155 per month. The investor just increased their Positive cash Flow by 58.33 per month (1213.33 minus 1155= 58.33). If this investor is disciplined enough to pay off entire principal balance on loan prior to Balloon payment, (usually 10 years) they win big. Every unscheduled payment they made lowered their monthly nut (P&I) putting more money in their pocket to use to pay off debt and realize their dream of owning the asset FREE & CLEAR. Now the disciplined saver can milk this CASH COW every month for the maximum amount of positive cash flow in the pocket.

I then asked the old man “if I don’t have any extra money to invest in unscheduled principal payments shouldn’t I lower my mortgage payments every month by getting involved with an adjustable rate mortgage loan? The old man smiled at me and said “if you were gambling who would you rather be – the player or the house? Naturally I said the house, historically over time the house always wins. The old man said no matter what you call it ; an ARM (adjustable rate mortgage) an AML (adjustable mortgage loan) or a VRM (variable rate mortgage) the adjustable rate mortgage is a mortgage loan that was designed by bankers aka “the house”, for bankers to guarantee one thing ; that they win the game of yield. Many years ago the lending

industry had a problem, they lent out trillions of dollars at low fixed rates of interest and when the rates shot up, the bankers wound up losing billions of dollars of profit, because a lot of their money was tied up in these lower yielding loans .In order to combat this problem the bankers came up with a creative solution they created the adjustable rate mortgage. Let me show you what I am talking about. If Dum Dum lending corp. lent out \$208,000 @ 7 % 30 yr they would gain in 30 yrs a profit of \$290,178.51 (see page #20). If prevailing interest rates shot to 10 % by the end of the year Dum Dum lending corp. if they lent out the same \$208,000 @ 10 % 30 yr would realize in 30 yrs a profit of \$449,446.40 * The bank would wind up losing \$159,267.89 (449,446.40 minus 290,178.51 = \$159,267.89) on only one loan because there was no mechanism in place to grab those extra yield dollars by increasing the interest rate on the loan until the coveted and much respected ARM rolled into town. It took the guesswork out of timing the market for the bankers. The bankers could now regulate their profits in a high or low interest rate market. The bankers no longer needed a psychic with a crystal ball to predict when rates would change all they needed with the ARM was a mathematician with a pen. The ARM loan is a *fixed* game; all the cards are stacked in the houses favor. When the rates go up so do you, when the rates go down so do you *or do you?*

The old man said, “For the average Joe or Jane the bankers made the ARM a very complicated loan to understand.” The bankers deliberately did this because as my father said “ in confusion there is lots of profit”. The bankers purposely designed a system so fundamentally difficult that the average person would have no clue whether or not their lender was cheating them. There are so many variables involved in figuring out this loan:

- 1) **Initial interest rate** – is this the actual rate of interest or was this a “Teaser rate”- a below average interest rate to lure customers in , but not used to make interest rate adjustments. This “Discount rate” pretty much guarantees your monthly payment at adjustment will go up regardless of the market; you paid an artificially low rate to begin with; you owe the lender for their generosity. What is the “prevailing “ or actual rate of interest at the start of the loan?
- 2) **Adjustment period-** the period between one rate change and the next is called the adjustment period.; with Arm’s the interest rate and monthly payment can change every 3 months, every 6 months, every year, every three years or every five years or some variation in between. The old man said “ You better keep your calendar and pen handy so you do not miss your period”. In a 3 year ARM, the rate can change once every 3 years. In a 3 month ARM, the adjustment period is every 3 months and the rate can change once every 3 months.
- 3) **Caps on monthly payment-** The maximum amount of money per adjustment period that the lender can adjust the mortgage payment. Basically , a limit on how much your monthly payment can be increased or decreased at each adjustment interval. Payment Caps do not limit the amount of interest the lender can earn , so they may cause negative amortization.

3b) **Lifetime cap on monthly payment-**The maximum amount of money, for the life of the loan that the lender can legally adjust the mortgage payment. Basically, a limit on how much your monthly payment can be increased or decreased for as long as you have the loan. These lifetime caps do not limit the amount of interest the lender can earn, so if rates shoot to the moon you may owe negative amortization.

*(see chart pg #5 : 10.0 – 30 yrs= 8.78 per 1000 / 208 X 8.78 = 1826.24 per month for 30 years. / 1826.24 X 360 = 657,446.40 gross minus 208,000 original principal balance = \$449,446.40)

- 4) **Caps on interest rate**- A limit on how much the interest rate can go up or down at each prescribed adjustment period.
- 4b) **Lifetime cap on interest rate**- A limit on how much the interest rate can go up or down for the entire life of the loan.
- 5) **Negative amortization**- Positive amortization is when your monthly payments are large enough to pay the interest owed and reduce the principal on your mortgage. Negative amortization is when your monthly payments are *not* large enough (usually due to caps on monthly payments) to cover the interest owed to the lender. The lender will not forgive this profit, instead the lender will conveniently add this interest cost to the unpaid principal balance. Translation: Even after making many payments on the loan, you could wind up owing more money than you originally borrowed. You could borrow \$208,000 and in 6 years you could owe \$215,000 or more.
- 6) **Index**- The index is the tool or the gauge that the lender uses at the adjustment period to increase or decrease the interest rate on your ARM .The index is like a compiled average of interest rate charges for a given financial sector. The index is a physical number published daily or weekly in most prominent newspapers. Your interest rate is “tied” to your index, which means when the index rate goes up, your interest rate, at adjustment time goes up with it.

The most common indexes are:

- [Constant Maturity Treasury \(CMT\)](#)
- [11th District Cost of Funds Index \(COFI\)](#)
- [London Inter Bank Offering Rates \(LIBOR\)](#)
- [Treasury Bill \(T-Bill\)](#)
- [12-Month Treasury Average \(MTA\)](#)
- [Certificate of Deposit Index \(CODI\)](#)
- [Cost of Savings Index \(COSI\)](#)
- [Certificates of Deposit \(CD\) Indexes](#)
- [Bank Prime Loan \(Prime Rate\)](#)
- [Fannie Mae’s Required Net Yield \(RNY\)](#)
- [National Average Contract Mortgage Rate](#)

Which one of the above indexes do you want attached to your ARM ? Is one index historically better than another one ? Some financial wonders suggest a loan tied to a *lagging index (like COFI)* is better when rates are rising, while others suggest that loans tied to an index like CMT is best during periods of declining rates. Who is right? Who is wrong? Do I specifically target a loan based on the past history of the index? Is the past history of an index indicative of its future performance? Do I pay less interest with certain indexes? The answers to these questions are not clear-cut; the only thing for sure is that nobody really knows, its anybody’s guess. Are there certain “bad” indexes that favor the lenders and certain “good” indexes that favor the borrowers? Who Knows!! You can only go back in time and historically plot how the index already moved not how it will move in the future. All the educated scholars& financial analysts can do is professionally guess.

- 7) **Margin**- the number of percentage points the lender adds to the index at the adjustment period to increase or decrease the interest rate on your ARM. Translation: To calculate new interest rate you add a “spread” on top of the index called a margin.

8) **Conversion option** – The ability to pay an extra fee in certain ARM's to change the adjustable rate mortgage to a standard fixed rate loan, usually at the end of an adjustment period.

The old man said this loan is a paperwork nightmare; at every adjustment period you would have to cross-reference multiple sources of information to accurately determine the validity of your new mortgage payment. If you had multiple properties with multiple loans and differing adjustment periods you could have a real mess on your hands.

WOW!! Very confusing to say the least- you probably need an MBA, a NY times and a strong stomach to swallow all of that information in one sitting. The average investor will just assume the bankers know better and that the numbers and fancy calculations the banks use to determine monthly payments are accurate. Most investors will hide behind their egos and never admit lack of comprehension concerning the ARM. Most investors are oblivious to the unknown perils of the seemingly innocent ARM. For example, an annually adjusted ARM for \$200,000 may start at 5 %, but a 6 % cap could allow it to go to 11% within four years. This would raise the payment from \$1073.64 to \$1904.65, an increase of \$ 831.01 per month. (An unexpected increase of this magnitude would destroy the investment value of the rental property)

The old man said, “For the average investor, this loan is”

- Too complicated
- Too much thinking involved
- Too much information to remember
- Too many layers of confusion to unravel
- Too stressful (constantly worrying about the changing terms of the loan)
- Too difficult to budget money & realistically figure out Positive Cash Flow on rental property. (Fluctuating mortgage payment at adjustment)
- Too easy to get fleeced by greedy bankers

The old man liked an investing system that was simple to do, easy to duplicate and not mentally draining; that's why he chose standard, no frills, straight laced easy to decipher vehicles to work with; namely the “meat & potato fixed rate amortized mortgage loan “ or the “interest only loan”. There is absolutely no confusion at all with these loans. The “meat & potato” loan is as easy as 1,2 and 3.

- 1) Loan amount
- 2) Term of loan
- 3) Fixed interest rate

The “interest only “loan is as easy as 1,2,3 and 4.

- 1) Loan amount
- 2) Term of loan
- 3) Fixed interest rate
- 4) Balloon payment due

There is no “teaser rate”, adjustment period, caps, index, margin or anything else that could cloud your investment mind, just “plain Jane “, basic, easy to follow and profit from mortgage vehicles. The old man said I built a small empire on the backs of these powerfully simplistic mortgage vehicles, and so can you if you heed my advice. His final parting words on the ARM was “... the ARM was born out of the necessity to qualify otherwise unqualified desperate first time home buyers for a home, *not* for the long term hold position of the sophisticated investors rental property.

- 2) “**Market equity**”- commonly known as Appreciation. The old man was very clear on his definition of Appreciation; **Appreciation-the gradual increase in value of real property through the natural course of events.** The old man said let me translate that for you: A property’s value goes up naturally, due to market conditions, not due to external factors like spending money on improvements or additions. If your house is worth \$300,000 and you invest \$100,000 to do an extension and now the property’s value has increased in value to say \$360,000, this \$60,000 increase in property value was *not* due to natural forces it was caused by an unnatural event called a construction project and therefore it is not appreciation.

The old man said, the laws of supply and demand naturally move the real estate market into and out of a **Seller’s Market** and a **Buyer’s Market**.

- **Seller’s Market-** Low supply of homes for sale in market & High demand from large supply of qualified buyers. Translation: 10 buyers and only 2 houses for sale. The large pool of qualified buyers fight over scarce supply of homes to buy, raising values and causing High Appreciation rates in the real estate market. A market favoring sellers. The seller can command Top dollar in this highly competitive marketplace. Bidding wars- pitting buyer vs buyer are common in this market. This is a great market for an investor looking to unload any undesirable rentals. The intense competition among realtors for listings makes the sellers market a great environment to sell in. The seller can guarantee a higher net sales price by negotiating hard with desperate realtors who need inventory (listings). In a sellers market , where listings are scarce, it is not uncommon for realtors to accept 4 % , 3% , 2% and even 1 % to sell your house. Some “flat fee” realtors will even work for less than 1 % , just to score the listing. In a red hot sellers market , some sellers have successfully bypassed realtors altogether and opted to sell on their own and pay \$0 commission.

In a sellers market its **all about the house**; whoever has the listing controls the game. The seller has the upper hand and all the leverage. The seller is not interested in creative deals or holding paper; they want all cash and they want to close yesterday if possible. The seller doesn’t care what defects a licensed engineer or home inspector, finds concerning the property; the price to the buyer is nonnegotiable or the seller will replace that buyer with a less discriminating buyer who will accept property as is. If the appraisal comes in too low, the seller won’t reduce price; the seller will require you to make up the difference with cash or find another buyer who will.

In a highly appreciating sellers market the most lucrative investment vehicle for investors is the no money down techniques. The investor ties up as many properties as possible & puts as little as possible down, gaining maximum leverage, and rides the appreciation wave to big profits. The investor is not concerned what the property is worth *today*, they will pay whatever it takes to gain control of a highly appreciating house in a hot sellers market. The investor is buying the house based on the future value of what the house can and will be worth *tomorrow*. This is a one-dimensional investing strategy that the old man called “appreciation only investing” or speculating. This investor can care less about **forced equity** or **positive cash flow** or **tax write offs**, they are only concerned with appreciation and short term flip profits. These investors are shortchanging the return on their real estate investment by only

investing short term for one reason (market equity) instead of long term , for four reasons, like the old man did : (1) forced equity, 2) **market equity** 3) positive cash flow & 4) tax write offs) For example, the short buck one dimensional “appreciation only” investor buys a house for \$260,000 and in 1 year of red hot appreciation sells it for \$290,000, making a short term \$30,000 dollar gross profit. The more experienced investor lazily stays in the investment longer and realizes much greater rewards by profiting from the benefits of all four dimensions of the real estate investment. The long term multi dimensional investor buys the same house for \$ 260,000 , and holds it for say 10 years , realizing the long buck profit of approximately \$289,621 (see real estate breakdown pg #) The old man said, “its simple math” the short term quick buck investor makes money, the investor with his eye on the long term becomes obscenely wealthy by investing for the long buck profits. The old man said, “don’t settle for the pennies of the short term hold, go for the big dollars of the long term hold”. The old man said, “don’t get me wrong, there are exceptions to every rule and the profit potential of the “Wreck” property with its inherited equity is one of them. The “Wreck” property (usually a foreclosure) is unique because usually the house was bought years ago, and is now in such disrepair, it disallowed years of long-term appreciation. In other words, while other similar homes in the area were naturally going up in value, this house maintained an artificially low value due to its poor condition. The smart investor gobbles up the dilapidated house, and activates the dormant long term appreciation by renovating run down property and in effect inheriting equity that would have taken years to acquire. Unlike “appreciation only” investing the investor does not have to wait for the market to go up in value prior to sale; the wreck already had the benefit of time to naturally increase its value. All you did was activate equity that was already there, but hidden by years of deferred maintenance by a neglectful owner. This is the only short buck game the old man liked to play. In essence you buy property at *yesterday’s* low price, fix it up and resell it at *today’s* higher price. A guaranteed winner for the investor that is familiar with the resale values of properties in their marketplace.

- **Buyer’s Market-** High supply of homes for sale in market & low demand from small supply of qualified buyers. Translation: 10 houses for sale and only 2 buyers. The small pool of qualified buyers have an overabundance of homes to chose from, this glut causes sellers to adjust price downwards to attract more offers, resulting in stagnant or low appreciation rates in the real estate market. A market favoring buyers. There are so many properties available that the buyer now has the upper hand when negotiating with the seller, the buyer is no longer locked in a bidding war with other buyers. This is a great market for an investor looking for a bargain priced property. The oversupply of listings makes the buyers market a great environment to invest in. You can score deals and even steals in a ripe buyers market. The sellers over inflated concept of value (what their houses are worth) have been stripped away by the reality of the buyers market. The sellers know the tide has turned. The days of double-digit appreciation are over. The neighborhood is littered with real estate signs; every other house is adorned with the placard FOR SALE.

The buyer can guarantee the lowest buying price by negotiating hard with multiple sellers desperate for their money. The buyer routinely submits multiple low ball offers on various properties hoping to land the most negotiable & flexible seller. The only hope the seller has of getting Top Dollar in a buyers market is to hope they have enough cash reserves and time to wait for the buyers market to run its course and for a new sellers market to begin. In a buyers Market the seller gets clobbered on price from the limited buyers and hammered on commission from the real estate industry. In a buyers market, where listings are plentiful, and its tougher to sell a house, it is not uncommon for realtors to charge upwards of 6 %, 7 %, 8 % and even 9 and over 10 % to sell your house.

In a buyers market its **all bout the buyer**; whoever has the buyer controls the game. The buyer has all the leverage to structure creative deals with sellers. The sellers are very receptive to negotiating favorable terms like holding paper or signing contracts subject to buyer selling their old house. The sellers will do whatever it reasonably takes to liquidate the property. In a buyers market, the engineers report or home inspection report is a powerful negotiating tool for the astute investor, because now the seller is actually willing to listen to and correct any defects or adjust the price accordingly. If the appraisal comes in lower than the contract price, the seller, fearful of losing the buyer, may reduce the price or offer some other incentive like a low interest seller held second to keep the deal alive.

In the low to no appreciating buyers market the most lucrative investment vehicle for investors is well priced long term rentals with favorable terms and short-term flips using a short sale. The investor is looking to buy rental properties with a substantial down payment, creating instant equity in investment and allowing a healthy positive cash flow to ride out the down market. The investor is basically in a holding pattern, obtaining well-priced assets and waiting for those assets to appreciate in value when the current buyers market eventually turns around and naturally flows into the sellers market. The smart investors are looking to acquire two to three bargain priced rentals in the buyers market and then sell two of the three rentals in the higher priced sellers market and pay off the outstanding mortgage on remaining rental, leaving the investor with a paid –in- full, free and clear asset; a rental property with a positive cash flow that pays them every month. The rental is your own personal “cash cow “ that you, the investor get to milk 12 times a year.

The high foreclosure rates associated with a buyers market make it fertile ground for the “short sale” mortgage flip. Basically the short sale is when a mortgage company “discounts” or takes less than what is owed to them in order to avoid the costly expenditures of a foreclosure action. If a mortgage company is owed \$400,000 on a property that was worth \$440,000 in a sellers market and is now worth \$380,000 in a buyers market, the company may be willing to accept \$320,000 cash from a buyer in order to cut any future losses. The investor can then fix up and flip property for a handsome profit. The short sale is a great vehicle for an investor to pick up a below priced rental property for a long term hold or a well priced investment property for a short term “quick profit” flip.

The “**seller’s market** “ & the “**buyer’s market**” are indirectly controlled by what the old man euphemistically called the “**greenspan effect**”(affectionately

named after Allan Greenspan). The greenspan effect is: interest rate changes indirectly control property values via affordability. Translation: the lowering or raising of interest rates affect the affordability of housing, thereby raising or lowering value of property. Further Translation: **Low interest rates** make homes more affordable for more people, creating greater demand to buy homes, increasing price people will pay to buy the home, leading to **high appreciation rate** in area causing a **“seller’s market”**. **Increasing interest rates** makes homes less affordable for more people, creating less demand to buy homes; decreasing price people can afford to pay to buy the home, leading to stagnant or **low appreciation rate** in area causing a **“buyer’s market”**.

Affordability is the issue. The same house will be worth one price in a sellers market and another price in a buyers market because the monthly mortgage payment per month will remain the same for both values. For example, if you bought a home in a buyers market for **\$300,000** , when interest rates were 10 % , and you put down 5% (\$15,000) ; you would borrow \$285,000 and your 30 year monthly payment of principal and interest would be **\$ 2502**. The same home in a sellers market, where interest rates are at say 6%, could fetch **\$438,950** because at 5 % down (\$21,947), you would wind up borrowing approximately \$ 417,000 and your 30 year monthly payment of principal and interest would be the same **\$2502**(GO FIGURE!).

As these figures clearly show the “greenspan effect “allows a house selling for \$438,950 to be just as affordable as a house selling for \$300,000 ; it just depends on the interest rate. In other words the same house worth \$300,000 in a soft buyers market with high interest rates is worth \$438,950 in a red hot sellers market with lower interest rates. The \$138, 950 difference in price does not affect the monthly mortgage payment. The mortgage payment is the same affordable \$2502 regardless of what price you pay. Affordability makes the same \$300, 000 dollar house worth \$438,950, because you need the same salary to comfortably pay a **\$2502** \$417,000 mortgage as you do to pay a **\$2502** \$285,000 mortgage. You need to know that there are two simultaneous values attached to one property , a “buyers market “ value & a “sellers market “ value. These values are established by the “greenspan effect”. The property is actually worth two prices at the same time , depending on the interest rate .The first value is what the property is worth at *Today's* interest rate and mortgage payment and the second value is what the property could be worth *tomorrow* when the “greenspan effect” kicks in when the interest rates are raised or lowered . In the above example the property is worth \$300,000(buyers market value) when interest rates are at 10 % and \$438,950(sellers market value) when interest rates are reduced to 6%. The old man said “ You need to understand this correlation between interest rates and property values in order to maximize your return as a successful long term real estate investor.” There is never a good time or bad time to invest in real estate ; only a **“seller’s market”** or a **“buyer’s market”**. You need to know the truth about real estate values. The old man said the value of real estate never stays constant, it is constantly changing based on the affordability of money in the marketplace. Every time the interest rate is adjusted a new property value is

created because the property has become less affordable (higher rate) or more affordable (lower rate) to the paying public. The “greenspan effect” shows :
As the interest rate swings up and down so does property value:

Rates are low -Prices are high- SELL

Rates are high- Prices are low- BUY

You want to buy when people are selling (“buyer’s market”) and sell when people are buying (“seller’s market”). Translation: You want to buy properties, at the “buyers market” price when there is a glut of people selling & high rates of interest (double digits) keep property values artificially low and sellers highly receptive to flexible and creative terms resulting in deals & steals from desperate sellers. When rates go back down in say , who knows, 3-7 years , sparking a sellers market , you refinance and get rid of that double digit loan or cash out and profit from increased property values of “sellers market”.

Further Translation:

BUY AT “BUYERS MARKET “ BARGAIN PRICE, WAIT FOR GREENSPAN EFFECT TO NATURALLY CONVERT MARKET TO SELLERS MARKET & SELL SAME PROPERTY AT HIGHER “SELLER MARKET” PRICE OR REFINANCE AT LOWER RATE AND HOLD FOR LONG TERM MONTHLY RESIDUAL INCOME.

The old man said, “now that you know how interconnected property values and interest rates are, you should realize that there is never a wrong time to buy real estate”. The price you pay is relative to the interest rates present at the time of your investment. A high price & a low price can be the same price depending on the affordability. For example, .if you were comfortable paying a \$2502 mortgage for a \$300,000 house you should be just as comfortable paying a \$2502 mortgage for a \$438,950 house. Affordability wise, both houses are the same value. You wont overpay by paying \$438,950 in a sellers market for the same house you can buy for \$300,000 in a buyers market. You didn’t underpay when you paid \$300,000 in a buyers market for the same house you would pay \$438,950 for in a seller’s market. In essence you paid the same affordable price.

Armed with this knowledge, you should now know that if you bought a \$438,950 house and the interest rates shot from 6%- 10%, you shouldn’t panic if your house loses \$138,950 in equity, and now is worth only \$300,000. This is supposed to happen. This is a natural event caused by the affordability or non-affordability of money in the real estate market. (aka greenspan effect). Naturally, when rates go back down, however long that takes; the property will recoup its value and once again be worth \$438,950 or more. The old man said, “money flowing into the real estate marketplace keeps values of real property in a constant flux, and only long term real estate investors can take full advantage of the high and low property values created by changing interest rates”. The old man said don’t try to figure out why or how interest rates go up or down, just know that when the powers to be adjust the rates the real property values in a given market are either raised or lowered, due to the cost of borrowing money. Translation: Appreciation is indirectly controlled by the “greenspan effect”.

3) **Tax Write-offs- Lucrative tax deductions / Legalized Loophole**

The Old Man said investing in real estate is like investing in any other business, “It doesn’t matter how much you make, it’s how much you keep that matters”. Real estate is a business well suited for legally avoiding paying heavy income taxes. The Old man said, **cash is king** with real estate you can **legally bury the green**. The tax laws and compliance requirements can be ambiguous and subject to different interpretations, so it is important to retain an accountant who can guide you through the ever-changing forest of IRS & State tax codes. Translation: A good accountant armed with the lucrative tax deductions of a rental property can legally shield you from taxes and keep more of your money in your pocket. You should become familiar with:

The Arsenal of deductions available to the rental property investor.

Operating Expenses of the rental are fully deductible

- Accounting fees
- Insurance premiums
- License fees
- Office supplies & expenses
- Exterminator
- Advertising costs
- Landscaper
- Janitorial service
- Property taxes
- Repair costs
- Legal fees
- Commissions paid
- Salaries (if any)
- Snow removal service
- Trash removal
- Utilities
- Telephone
- Property management fees (if any)
- Cost of credit reports, criminal checks
- Misc. supplies
- Etc...

Mortgage Interest- the interest on the rental property is fully deductible.

Amount Financed	\$208,000.00			
Years	30			
Interest Rate	7			
Monthly Payment	\$1,383.83	Bank Profit	"Forced Equity" Our Profit	
Month	Payment	Interest	Principal	Balance
1	\$1,383.83	\$1,213.33	\$170.50	\$207,829.50
2	\$1,383.83	\$1,212.34	\$171.49	\$207,658.01
3	\$1,383.83	\$1,211.34	\$172.49	\$207,485.52
4	\$1,383.83	\$1,210.33	\$173.50	\$207,312.02
5	\$1,383.83	\$1,209.32	\$174.51	\$207,137.51
6	\$1,383.83	\$1,208.30	\$175.53	\$206,961.99
7	\$1,383.83	\$1,207.28	\$176.55	\$206,785.43
8	\$1,383.83	\$1,206.25	\$177.58	\$206,607.85
9	\$1,383.83	\$1,205.21	\$178.62	\$206,429.23
10	\$1,383.83	\$1,204.17	\$179.66	\$206,249.57
11	\$1,383.83	\$1,203.12	\$180.71	\$206,068.87
12	\$1,383.83	\$1,202.07	\$181.76	\$205,887.11

(\$14,493.06)

The bank profit portion (red column) of your monthly mortgage payment is fully deductible. In this example the rental property investor gets to write off the full \$14,493.06 on their annual tax return.

Points

Any points paid on any mortgage secured by the rental property are deductible over the life of the loan. For example, if you obtain a \$208,000 loan with a 30 year term and you pay 1 point to obtain the loan, you can write off \$69.33 a year over the 30 year period for a total of \$2080. If you sell rental, and pay the mortgage off early, you can deduct all unused points in that year.

Closing costs- the closing costs associated with the **purchase** of the rental property are deductible in the year of the purchase.

- Title insurance
- Title fees
- Appraisal
- Application fee
- Recording fees
- Etc....

The old man said, you should check with your accountant because certain closing costs associated with a **refinance** on the rental property are deductible as well

Depreciation- “Loss on paper”

The government determines how many useful years your rental property has before wear and tear, age or obsolescence should force you to replace the structure. The IRS then allows you to depreciate or “write off“ the rental property over its useful life by taking a “paper loss” for a set number of years. Currently, the IRS allows residential rental properties to be depreciated over 27.5 years and commercial rentals to be depreciated over 39 years. For example, if you purchase a residential rental property in mid January for \$260,000 you have 27.5 years to write off the cost of the rental property structure minus the land it resides on. The land where the rental property is located is worth \$52,000 (approximately 20 % of purchase price). The building is worth \$208,000. You have a \$208,000 .deduction over a 27.5 year period of time. The rental property structure is depreciated by equal amounts annually over the 27.5-year period. (\$208,000 divided by 27.5 = \$7563.63 per year paper loss)

Since you purchased the rental property in January, the IRS rules allow you to write off 11 ½ months of depreciation in the first year or \$7248.48, ½ month of depreciation for January and 11 full months of depreciation for the remainder of the year. For the next 26.5 years you would deduct \$7563.63 per year and in the 28th year you would write off the remaining ½ month of depreciation, \$315.15, in the final year.

Translation- Even though your rental property can appreciate in value year by year, the government gives you a preset number of years to depreciate the rental property and take a “paper loss” on your taxes.

Capital Improvements- Major improvements to the rental property like a new roof, new siding, a dormer or extension, etc...are subject to the same depreciation schedule as above. Capital improvements to a residential rental property are depreciated over a 27.5-year period of time. Capital improvements to a commercial rental property are depreciated over 39 years.

Personal property- The rental property investor can write off some personal property items (items which are not permanently attached to the land or improvements) like a dishwasher, microwave, washer, dryer, furniture, lawn mower, snow removal equipment, etc.. The depreciation schedule on personal property can vary, a recovery period of 5,7,or 10 years could be used ; you should check with your accountant to determine the proper recovery periods for personal property.

The Old Man said, don’t fall in love with your tax deductions, they could be “Here today, Gone tomorrow”, that’s why you should never invest in real estate just for tax purposes. The politicians are forever changing the real estate landscape by changing deductions or wiping out certain write offs or adding newer more complicated tax codes and compliance requirements. The old man cited credit card deductions and depreciation schedules as good examples. The old man said prior to 1986, the best way to buy a rental property was using credit cards as your primary source of down payment money, because the interest charges were fully deductible. This lucrative tax saving door was abruptly closed in 1986 with the passing of The Tax Reform Act of 1986, which among other things wiped out interest deductions on credit cards. The investor who borrowed heavily on credit cards and counted

on this deduction to justify their investment in a rental property were rudely awakened when this write off was arbitrarily eliminated. The old man said, “that’s why you should never invest in real estate based solely on the tax consequences”. The other three reasons; forced equity, market equity and positive cash flow are equally if not more important in justifying your rental property investment.

The old man said, when I first started investing in rental properties in the late 70’s, early 80’s the depreciation schedules were very lucrative for the rental property investor:

- 1-1-81 to 3-15-84 - 15 year schedule
- 3-16-84 to 5-8-85 - 18 year schedule
- 5-9-85 to 12-31-86 - 19 year schedule

In 1987, when the government decided in it’s infinite wisdom to double the time it took to depreciate rental property (from 15 years to 27.5 years effective 1-1-87 to present) the old man didn’t stop investing in rentals because the tax laws suddenly changed. The old man knew full well the financial merits of investing in real estate for all four reasons, not just one.

The old man said, even if the government took away all the deductions and write offs associated with rentals there still exists a legalized loophole to avoid paying any income taxes(capital gains) on the profit generated from the sale of the rental property, the 1031 Tax deferred Exchange. The 1031 is the sacred cow of the rich property owning politicians. The 1031 Exchange is the vehicle that legally allows the rich to get richer in the forum of real estate.

The Mechanics of a 1031 Tax deferred Exchange

- 1) All monies to be exchanged must be deposited with a non-interested third party called a qualified intermediary (QI) or exchange accommodator. The key words here are non interested, the QI cannot be your best friend or your lawyer or your accountant. In order to avoid any conflict with the IRS a non-partial unbiased unrelated third party should be retained. The typical intermediary fee for an exchange is \$5-\$10,000 or more depending on the complicity of the transaction.
- 2) The QI can facilitate many different types of exchanges:
 - **Build to suit / Improvement-** The QI holds title to the replacement property on behalf of the property seller, while improvements are done to the replacement property. Commonly known as an Improvement exchange.
 - **Delayed-** In a delayed exchange, typically known as a Starker exchange your relinquished property (your old property) is exchanged for a promise from someone (most likely a facilitator company) to acquire a replacement property for you at a later date.
 - **Reverse-** an exchange where you buy the replacement property first and then you sell your relinquished property (your old property) afterwards.
 - **Simultaneous-** the sale of the relinquished property (your old property) and the purchase of the identified replacement property takes places simultaneously.
 - **1033 tax deferred exchange-** a special exchange exists when eminent domain(the legal right of the government to seize your property for just compensation) is involved in the sale of your relinquished property (your old property). You have up to 2 years to find a suitable replacement property in this exchange.
- 3) 45 day Identification Period- the investor has 45 days from the closing of the property to select and identify property or properties to purchase and 180 total days to close the purchase of the identified property /properties. Since this is a real estate transaction, this selection process has to be in writing (Statue of Fraud). The Old Man said remember weekends and holidays count so in

actuality this identification time period can be much sooner depending on the time of year you do the exchange. Fair warning the old man said, you should protect your best interests and identify more than one property for your exchange, just in case your deal for the replacement property falls through. By code you can identify up to three properties regardless of value and you don't have to buy all three.

4) Like Kind- the property/ properties that you exchange must be of "like kind". Like kind is real estate or other tangible property that is similar in nature or classification. Translation: Can you exchange raw land for a 10 unit apt building? . Yes you can they are both classified as real estate and therefore are of "like kind". Like kind property cannot be a primary residence or a second home it must be for business or investment purposes

5) "Boot"- any non qualifying property (property that is not "like kind") received from a 1031 Exchange. "Cash boot" and "Mortgage boot" are the most common types of "boot". "Boot" is fully taxable. For example, you exchange your \$500,000 rental property for a \$470,000 rental plus \$30,000 cash. The \$30,000 would be "cash boot" and subject to taxation.

The Old man said the 1031 Exchange has been a part of the IRS tax code since the roaring 20's; the very beginning of income taxes in America. The 1031 applies only to property held for commercial, business or investment purposes, your primary residence is ineligible.

The old man said, don't despair, there also exists a legalized loophole for avoiding paying income taxes on your primary residence when you sell it; **the Internal Revenue Code 121 Principal Residence Exemption**. You can legally exclude up to \$250,000 on the gain of the sale of your primary residence if you are single and up to \$500,000 on the gain at sale if you are married if "during the 5 year period ending on the date of the sale, such property was owned and used by you as your principal residence for a period aggregating 2 years or more ." Translation: You do not have to actually live in house to get exemption, just prove you lived in it 2yrs out of the last 5 years prior to sale. The IRS rules for this exemption are very clear, you must satisfy both the ownership test and the use test for the 2-year residency requirement.

The ownership test is easy; you must be on the deed to the property for at least 2 years. The residency requirement is a little more stringent: Too many investors tried to get in on the fun so the IRS established certain guidelines to determine eligibility.

For your house to qualify as your principal residence the IRS must verify :

- a) This house is the place you always plan to return to when you are away
- b) This house is the address you used to register to vote
- c) This house is the address that appears on your driver license
- d) This house is the address you use when filing your official tax returns
- e) This house is the address of record where your kids attend school

On a case by case basis the IRS could be flexible on the occupancy test if the sale of the house was induced by :

- a) Health reasons-
- b) Change in place of employment
- c) Unforeseen circumstances
 - 1) Death
 - 2) Divorce or legal separation
 - 3) Multiple births
 - 4) Unemployment
 - 5) Change of employment

- 6) Condemnation, seizure or other involuntary conversion of property
- 7) Damage to property due to man made or natural disaster, terrorism or acts of war
- 8) Any other circumstances the IRS commissioner determines are unforeseen.

The Old man said rentals held in a corporate entity offer even greater tax deductions as well as legal protection from certain lawsuits. He said, “If you are looking to hide your wealth and grow silently rich, under the radar of public scrutiny you must find the business structure to accommodate this lofty endeavor. That structure is the corporation.” If the property is in a corporation name technically you do not own it, the corporation which is considered a separate individual from you, owns it. The corporation like the individual has it’s own unique identifying number that separates it from you and the rest of the world. You have a nine-digit social security number; the corporation has a nine digit Federal tax ID number. The corporation can serve as a legal and financial buffer between you and what all the litigious people in the world want – your assets. You can legally distance yourself from your assets (rentals aka “cash cows”) and hide your wealth with a corporate entity. The old man said no one in this “sue crazy” society should have the right to know the extent of your accumulated assets (like how many rentals you own), they should all be safely parked in corporations. The old man said when you shed your ego and place your assets in a corporation it allows you to have direct control of your assets without the financial and legal worries of personal ownership. The Old man said, the amateur investor who holds the rental property in their own personal name (probably for bragging rights) leaves themselves open for a massive lawsuit. The corp. provides a veil of protection from avaricious lawyers looking to separate you from your money. The old man said, if your rental was in your own name and you got in a car accident and killed someone, you could possibly lose your asset in a wrongful death lawsuit. The rental held in a corporation name, especially with multiple owners, is a little more difficult to obtain in a lawsuit since legally you do not own this asset. The old man said, don’t get me wrong, the corporation is not Full proof protection from lawsuits. The lawyers could sue for the shares of the corporation that you personally own and still get the asset or if you committed a felonious act the corporate veil could be pierced and they could get your asset. The old man said the most important reason to hold rentals in the corporate structure is the added tax write offs, the legal protection is an added bonus.

The corporation is the perfect vehicle to hide your money and protect your wealth. The Old man said “if you have a Pension Walker it is mandatory for liability purposes and financial reasons to let a holding corp. own this valuable source of passive income. “ What type of corporation you use to shield your wealth from the roving eyes of the general public depends on you and your accountant. Some accountants swear that the Limited Liability Corp. is the best option to hold real estate, while others prefer an S Corp or a C Corp. The Old man was partial to the S Corp, it didn’t allow “double taxation” of his profits, if any profits somehow existed after the lucrative tax write offs of the rental property were figured in. The old man said, the corp. not only allows you to hide the asset, it also allows you to legally hide the income generated from the asset by funneling the revenues (positive cash flow) through a corporation replete with deductible expenses. The old man said, with the aid of the corporation you can legally deduct a host of your living expenses like; car repairs, car lease, cell phone, health insurance, fun business trips to exotic locations, meals and entertainment,

gas, educational seminars etc... The corporation affords you the anonymity you need to privately and surreptitiously build your real estate empire.

The old man said for the ultimate form of anonymity some investors chose the C corp. Unlike other corp. structures, the C corp. pays its own taxes, there is no Schedule E on your personal tax return that can be traced back to your corporation and the assets it controls. Translation: Even if some one had access to your personal tax return, they would have no clue you owned other assets (like rentals) in a C corp. because you are not required to divulge this information on your personal return. Your own wife or husband wouldn't even know unless you volunteered this information. Other corporations or business structures leave a paper trail directly back to you. Your personal tax return is the key that unlocks the door. The IRS requires business owners of certain business structures to report profit and losses of their business on their personal tax return.

The sole proprietorship business structure has the Schedule C, the partnership business structure has Schedule E part 2, the K-1, and if you have a 25% or more interest in corp., the 1065, the S corp. has Schedule E part 2, the k-1 and if you have a 25% or more interest in corp., the 1120 S. The C corp. doesn't invade the sanctity of your privacy by requiring disclosure of corp. activities on your personal tax return, it is invisible to untrained eyes.

As a side note, the Old Man said "when you payoff your primary residence, you should further protect your financial privacy by obtaining a Line of Credit on it, so no one has to know the house is paid off". If your house was paid off and worth \$600,000 and you obtained a \$300,000 Line of Credit on it, a \$300,000 lien would be recorded on the property even if there was no balance on the loan. Translation: The whole world would see a \$300,000 debt registered against you even though you owe nothing. A great way to masquerade the fact that a) the house is paid off and b) that you are not struggling with a heavy mortgage like the rest of the lively middle class. The Old man said the added kicker is the Line of Credit, if used wisely can bankroll your short term real estate investments, like the occasional quick flip.

4) Positive Cash Flow- "The Pension Walker's"

The old man said positive cash flow is the money left over per month after paying out all monthly property expenses on investment property. Technically, the tenant pays you rent; you pay the mortgage (Principal & Interest) and the property taxes (T) and the homeowner's insurance (I) on the rental (PITI) and any monies remaining after paying these expenses is your monthly positive cash flow. Translation: Positive Cash Flow is Rent Roll minus Total Monthly Expenses. For example:

RENTAL PROPERTY

Home Price	\$260,000.00
Down Payment	\$52,000.00
Amount Financed	\$208,000.00
Years	30
Interest Rate	7
Monthly Payment	\$1,383.83

Mortgage Payment -	\$1383.83
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60

Total monthly expenses-	\$ 1943.83
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 556.17 Per Month

Translation: You rent out your investment property for \$ 2500 per month and after using this money to pay your mortgage, property taxes and insurance you have extra spendable money, namely \$556.17. Mooooo Mooooo , every month you get to milk this “cash cow” for over five hundred and fifty six dollars. Whenever the old man had a rental with a positive cash flow (which was all the time) he used to call it a “cash cow”, and every month when he collected rent he referred to it as milking the cow. The old man called this extra money per month that he milked from his “ cash cow” rentals the “the king’s slush fund”, the reserve money that the old man used to finance his surreptitiously lavish lifestyle. The old man said , “ the smarter you invest the larger your slush fund becomes’ .An average investor could easily attain a \$2000-\$5000 per month slush fund within a 10-15 year investment period. The superior investor can retire early by collecting monthly what some people make annually. The old man knew what he was talking about; he was putting \$ 10,000 clear a month in his pocket back in the late 80’s.The old man quickly became addicted to a new habit, namely getting paid *not to* work hard by collecting rent. The old man discovered that collecting cold hard cash can be even more addictive than his other vices; women, coffee and cigarettes. **Positive Cash Flow** was the reason the old man was semi retired at 43 years old. The old man never liked people to openly know he had money, he always cried poverty, even on the first of the month when his pockets were bulging with wads of fresh cash from his recently milked “cash cows”. If you were after his money, he always threw you off the scent by claiming massive bills & heavy expenses, “ casualties “ , he would half heartedly say of being a struggling landlord. . He never liked strangers to know how lucrative being a landlord really was; he reserved that information for fellow investors and close friends. The only people that needed to know how much the old man made was the Old man, his accountant and his silent partner the government. The old man said, Increasing Positive Cash Flow is the end all goal of real estate investing. It is the reason you learned about the other three areas of real estate (forced equity, market equity& tax write-offs) The mission from day one of real estate investing is to use this collective knowledge to increase your positive cash flow and allow you to live like a king off of the passive stream of monthly income generated by your tenants.

Increasing Positive Cash Flow

- a. Amortization/Forced Equity- the “Do Nothing” system of Guaranteed future Positive Cash Flow, just pay your standard “Meat & Potato fully amortized fixed rate mortgage loan” every month and let the natural process of amortization wipe out your loan and increase your positive cash flow.

For example:

RENTAL PROPERTY	
Home Price	\$260,000.00
Down Payment	\$52,000.00
Amount Financed	\$208,000.00
Years	30
Interest Rate	7
Monthly Payment	\$1,383.83

Mortgage Payment -	\$1383.83
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 1943.83
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 556.17 Per Month

This rental property is generating a \$556.17 per month positive cash flow. All you have to do to increase the positive cash flow is "Do Nothing" , just make all your mortgage payments (360) and amortization will naturally wipe out loan in 30 years , increasing the positive cash flow per month by \$1383.83 by eliminating the mortgage expense per month . In 30 years this property will generate a positive cash flow of \$556.17 plus \$1383.83= **\$1940 per month.**

Mortgage Payment -	\$ 0
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 560
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 1940 per month

The Old man said the end result of Forced Equity is a paid off house which represents a rental property's maximum monthly positive cash flow dollars.

- b. **Accelerated Amortization/ Forced equity**- the "Pre-pay" system of Guaranteed future Positive Cash Flow, all you do is accelerate the payoff of your standard amortized "Meat & Potato" loan by making unscheduled principal payments and wiping out loan sooner, increasing the positive cash flow, earlier than scheduled. Translation: You don't have to wait 30 years for your increased positive cash flow, you can speed up the amortization timetable with pre-pays and get the same result sooner; a \$1940 maximum positive cash flow . In the above example if we gave a \$5,000 unscheduled principal payment on the loan we could arrive at our goal of increased positive cash flow in 28 years instead of 30 years. (See page # 20). The more money you invest into your forced equity column of your amortization schedule the quicker you get to enjoy the benefits of your increased positive cash flow. The old man said if you do not need the extra \$556.17 a month now, reinvest it into pre-pays, pay off rental sooner and retire early.

c. Interest Only Non amortized loan Pre-Pays

Unlike amortized loans, when you make an unscheduled principal payment on a interest only loan the monthly mortgage payment gets reduced immediately, you do not have to wait 30 years like the "Do Nothing" system, your positive cash flow increases by the next month.

You get instant satisfaction from your pre-payments in an interest only loan.

For Example;

RENTAL PROPERTY

Home Price	\$260,000.00
Down Payment	\$52,000.00
Amount Financed	\$208,000.00
Years	
Interest Rate	7
Monthly Payment	\$1213.33

Interest only payment is \$1213.33 (\$208,000 X 7%= \$14,560 / 12 = 1213.33 per month)

Mortgage Payment -	\$ 1213.33
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 1773.33
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow	\$ 726.67

You make a \$5000 unscheduled principal payment on loan it changes the monthly mortgage payment from **\$1213.33 to \$1184.16**, instantly increasing your positive cash flow on rental by \$29.17 per month.

RENTAL PROPERTY

Home Price	\$260,000.00
Down Payment	\$52,000.00
Amount Financed	\$203,000
Years	
Interest Rate	7
Monthly Payment	\$1184.16

After \$5,000 unscheduled principal payment Amount financed is now \$203,000 and newly calculated interest only payment is \$1184.16 (\$203,000 X 7% = \$14,210 / 12 = 1184.16)

Mortgage Payment -	\$ 1184.16	
Property Taxes (6000)	\$ 500 (6000 / 12)	
Homeowner's insurance- (720)	\$ 60	
Total monthly expenses-	\$ 1744.16	
Rent Roll- (monthly rent)-	\$ 2500	Positive
cash flow-	\$755.84	

By the next month the \$5,000 pre-pay has increased the positive cash flow from \$726.67 to \$755.84.

- **Refinance Your Way to Increased Positive Cash Flow-** If you bought a rental property when prices were low but interest rates were high (usually a buyer's market) you could increase your positive cash flow by refinancing property when interest rates eventually go down.

For example;

RENTAL PROPERTY

Home Price	\$260,000.00
Down Payment	\$52,000.00
Amount Financed	\$208,000.00
Years	30
Interest Rate	10
Monthly Payment	\$1826.24

Mortgage Payment -	\$ 1826.24
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 2386.24
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow	\$ 113.76

When interest rates are at 10 % you have a meager positive cash flow of \$113.76 for the month

RENTAL PROPERTY

Home Price	\$260,000.00
Down Payment	\$52,000.00
Amount Financed	\$208,000.00
Years	30
Interest Rate	7
Monthly Payment	\$1,383.83

Mortgage Payment -	\$1383.83
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 1943.83
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 556.17 Per Month

When you refinance your 10 % loan down to a 7 % loan you increase your positive cash flow from \$ 113.76 per month to a \$556.17 a month, an extra \$442.41 per month.

- **Sell/Trade Your way to Increased Positive Cash Flow-** If you bought a rental property when prices were high but interest rates were low (usually a seller's market) you could increase your positive cash flow by waiting for enough equity to build up and sell or trade your way to a higher positive cash flow.

Home Price	\$260,000.00
Down Payment	\$52,000.00
Amount Financed	\$208,000.00
Years	30
Interest Rate	7
Monthly Payment	\$1,383.83

Mortgage Payment -	\$1383.83
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 1943.83
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 556.17 Per Month

If this \$260,000 rental appreciated in value (in 10 yrs.) and was now worth \$420,000 you could sell it for \$420,000 and use the proceeds to put a larger down payment on another rental guaranteeing you a higher positive cash flow. OR If you owned two rentals you could sell one to pay down the mortgage or payoff the mortgage on the other one.

Sales Price-	\$420,000
Mortgage balance remaining after 10 yrs of amortization	\$178,489.62(see pg 18)
Closing costs associated with sale- tax, attorney fee, adjustments, recordation fees, etc...	4% broker fee- \$ 16,800 Transfer \$ 4200
	Sub total Expenses \$ 199,489.62

Proceeds \$ 420,000 minus \$199,489.62= \$220,510.38

You now reinvest your proceeds into a \$300,000 rental and put a 50% down payment (\$150,000) and increase your positive cash flow.

Home Price	\$300,000
Down Payment	\$150,000
Amount Financed	\$150,000
Years	30
Interest Rate	7
Monthly Payment	\$997.50

* (Check Amortization Chart \$150,000 @7%=150 X 6.65 =\$997.50)

Mortgage Payment -	\$997.50
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 1557.50
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 942.50 Per Month

You just increased your monthly positive cash flow from \$556.17 a month to \$942.50 a month a \$386.33 per month increase and you have \$70,000 left over (\$220,000 minus \$150,000) for buying closing costs , misc. repairs or seed money for another rental property.

The Old man said the best way to accomplish this feat is Tax Free via the 1031 Tax Deferred Exchange. If done properly you can indefinitely avoid the expense of any tax liability (no capital gains) associated with the sale. In essence you are perpetually deferring the tax on the gain by reinvesting the proceeds of sale back into another similar property or properties with a higher positive cash flow. Technically you are not *selling* your property; just exchanging the equity in one property for the equity of another property or properties.

- **Protest Property Tax/Comparison Shop Homeowner's Insurance to Increase Positive Cash Flow-** By lowering expenses on rental you increase positive cash flow per month.

Property Tax- Every year you have the legal right to try to lower the amount of property taxes that you pay on your rental by protesting your property tax bill. The goal is to challenge the tax bill by finding similar properties to yours that are paying less property tax than you are. The old man strongly recommended that you use a professional tax reduction service. He said, they do all the legwork and only get paid if and when they save you money. It cost you absolutely nothing to explore this expense saving option. If they do not lower property taxes initially, you should make it a yearly habit to contact them; you never know when future circumstances could change in your favor and you are granted a property tax reduction.

For Example:

Mortgage Payment -	\$1383.83
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 1943.83
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 556.17 Per Month

If you successfully reduce property tax bill down to \$5000 from \$6000 you gain an extra \$83.00 per month of positive cash flow.

Mortgage Payment -	\$1383.83
Property Taxes (6000)	\$ 416.66 (5000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 1860.49
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 639.51 Per Month

You have increased your positive cash flow from \$556.17 a month to \$639.51 by successfully protesting your property taxes & lowering your property tax expense on rental.

The Old man said, another way you could reduce your property taxes and subsequently increase your overall positive cash flow in life is through property tax exemptions on your primary residence. (where you live). An exemption is a reduction in property taxes for qualified property owners. Most exemptions are for primary residences only, non-owner occupied rental properties usually are not eligible. The old man said, even though property tax exemptions usually do not apply to rentals, they get an honorable mention, since most investors own their own homes and could use the savings to increase their overall positive cash flow in life.

The old man said, Do the research son, if you own a home you owe it to yourself to take full advantage of any & all property tax reducing Exemptions that you are qualified for. (Researched 2003) Some common Property tax Exemptions:

- **STAR**- New York State School Tax Relief Program- provides reduction in school tax portion of property tax bill for all New Yorker's who own their own home and use it as primary residence.

Two parts to STAR Program:

- 1) **Basic Star**- reduction in school taxes for general public- no age or income requirements. Average tax savings per year - \$200
- 2) **Enhanced Star**- reduction in school tax for seniors- age and income requirements apply- must be 65 or over & make \$66,050 or less to qualify.

Average tax savings per year- \$350

- **Veterans Exemption**- provides reduction in property taxes for a qualified veteran, the unmarried surviving spouse of a qualified veteran or a Gold Star parent (the parent of a child who died in the line of duty while serving in the US armed forces during one of the periods below) Primary residence only. No income requirements. Need veteran's DD-214 (separation papers) or proof of discharge.

You are a qualified veteran if you served your country during one or more of the following periods of war or conflict;

Mexican Border Period (5/9/1916 - 4/5/1917)

WWI (4/6/1917-11/11/1918)

WWII (12/7/1941- 12/31/1946)

Korean War (6/27/1950-1/31/1955)

Vietnam War (12/22/1961-5/7/1975)

Persian Gulf Conflict (commencing 8/2/1990)

Average tax savings per year –3 levels of benefits

- 1) 15 % of property's assessed value (or \$3,600 whichever is less)
- 2) Additional 10 % (or \$2,400 whichever is less) if you were in actual combat
- 3) Additional exemption applies if you saw combat and got disabled. (The exemption can go as high as \$12,000 for disabled vets)

- **Senior Citizen Homeowner’s Exemption (SCHE)**- provides reduction in property taxes for senior citizens on limited income. Must be 65 and over. Primary residence only. Adjusted gross income must be less than \$32,400. Must own house for the last 12 months prior to applying for exemption.(exceptions to 12 month rule can be granted). The amount of exemption is determined by a sliding scale of income; the lower the income the higher the exemption. Translation: the less you make, the less property tax you pay. In NY, the sliding scale is as follows:

IF the Owners’ Income is Between	SCHE will reduce The assessed value by
\$0 and \$23,999	50 %
\$24,000 and \$24,999	45 %
\$25,000 and \$25,999	40 %
\$26,000 and \$26,999	35 %
\$27,000 and \$27,899	30 %
\$27,900 and \$28,799	25 %
\$28,800 and \$29,699	20 %
\$29,700 and \$30,599	15 %
\$30,600 and \$31,499	10 %
\$31,500 and \$32,399	5 %

(WWW.nyc.gov)

As a side note the old man said, the biggest complaint that seniors have with the current property tax system is the school tax. Most seniors feel that since they have no children matriculated in school they shouldn’t be unjustly burdened with a heavy tax for a service that they do not receive. The old man always took time out of his busy life to educate seniors about the folly of their thinking. He would tell them, “you are not the only group of people that pay taxes for services that are not received “. There are 2 other notable groups of people who equally contribute to the school tax coffers and receive minimal or no benefit:

- 1) **Optional education group** - the ever growing group of parents who forgo public education for at home schooling or religious education , like Catholic school. Theses parents pay school taxes and their children do not even attend the school that there taxes subsidize. In essence these parents pay twice, they pay school tax for public education plus they have the financial burden of paying for their child’s private education. Unlike the seniors there exists no exemption to reduce this burden. The old man said the government has been toying with ways to correct this injustice , like implementing a tax credit but as of late this group has no relief from their “double bill”.
- 2) **Walkers**- the group of residents who live too close to the school to get public busing. They pay the same school tax bill as everyone else yet they have to spend their gas money and time to physically drop off and pick up their kids from school while other parents get the benefit of public busing. The walker has to rearrange their schedule to accommodate the lack of convenience of a bus. The walker group and their children are subjected to fumes emitted by cars lined up at drop off points, frigid cold, rain, snow, sleet, ice etc...The old man said there should be a tax exemption for walkers, they unfairly pay taxes for buses that they do not get to use.

- **Disabled Homeowner's Exemption (DHE)**- provides reduction in property taxes to low income disabled homeowners. Primary residence only. Applicant must have provable disability. Adjusted gross income cannot exceed \$32,400.

Average tax savings per year- 5-50% of property's assessed value depending on income.

- **Home Improvement Exemption**- the real property tax exemption for capital improvements to residential property.(usually 1-2 family properties owned for more than 5 years) Major renovations increase assessed property value and raise property taxes. This exemption can prevent the payment shock associated with the massive property tax increase of a major capital improvement like a dormer or extension. Instead of raising your property taxes all at once, the assessor slowly increases your tax bill over a set number of years. Each locality is different; you need to do your own research to determine eligibility requirements. In Suffolk County, if you qualify for the HI exemption they give you 8 years to adjust to your newly increased property tax bill.

<u>Year</u>	<u>Exemption %</u>
1	100
2	87.5
3	75
4	62.5
5	50
6	37.5
7	25
8	12.5

Translation:

Year # 1 - you pay 0% of your inevitable property tax increase because you are 100% exempt from paying your increased tax obligation, Year # 2- you only pay 12.5 % of your inevitable property tax increase because you are 87.5 % exempt from paying your increased tax obligation, Year # 3 you only pay 25% of your inevitable property tax increase because you are 75 % exempt from paying your increased tax obligation , etc.. And so on for subsequent years.

- **Fire Dept/EMT**- provides reduction in property taxes for volunteer firefighters and ambulance workers. Primary residence only. No income requirements. Do your research; the amount of exemption can vary from town to town and county to county. In Suffolk County where I live the exemption is 10 % of assessed value. The exemption is only available to volunteer firefighters and volunteer EMTS' who have been certified enrolled members for a minimum of 5 years. After 20 years of dedicated volunteer service the 10 % exemption is usually granted for life.

Homeowner's Insurance- Every year like clockwork the Old man would conduct an insurance check-up on his rentals. His mission every year was always the same: save money by shopping around for the best coverage with the lowest possible premium payments. He conducted this mission at the same time each year; renewal time, when the insurance bill is fresh in your mind and you are least likely to forget. The old man said that there are a number of ways to save money on homeowner's insurance:

- 1) **Lower Premiums-** Find a company that will give you the same coverage for less money.

Mortgage Payment -	\$1383.83
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (720)	\$ 60
Total monthly expenses-	\$ 1943.83
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 556.17 Per Month

Through cost comparison-shopping you reduce ins. bill down to \$600 yr. from \$720 yr. , you gain an extra \$10.00 per month of positive cash flow.

Mortgage Payment -	\$1383.83
Property Taxes (6000)	\$ 500 (6000 / 12)
Homeowner's insurance- (600)	\$ 50
Total monthly expenses-	\$ 1953.83
Rent Roll- (monthly rent)-	\$ 2500
Positive Cash Flow-	\$ 566.17 Per Month

You have increased your positive cash flow from \$556.17 a month to \$566.17 a month by successfully shopping and subsequently lowering your insurance expense on your rental.

The old man issued a stern warning regarding insurance, “never jeopardize good coverage for a low premium, always compare apples to apples, use your old declaration page as a guide when shopping coverage and getting new quotes”. You never want to have cheap insurance because of inadequate coverage. The old man said “ If disaster strikes, you’ll be more concerned about how good your insurance policy is *not* how low the premium is “, so shop wisely. The little pennies you save on insurance today , could cost you big dollars tomorrow in the event of a claim. . The old man said never make the amateurish mistake of saving money by **underinsuring** your rental with a “fire only” insurance policy. This cheap insurance policy covers damage to the rental property but leaves you vulnerable to the more costly damages of bodily injury and property damage to others. The Old Man said, in this litigious society it is in your best interest to be *properly* insured , to protect the financial soundness of your rental property investment. If a chunk of your building falls off and kills someone you could be liable for millions in damages. You’ll wish you spent the extra money **now**, instead of losing all your money **later**.

- 2) **Raise Deductible-** a deductible is the amount of money you have to lay out first before your insurance kicks in. If you have a \$200.00 deductible on your insurance policy, you agree to pay \$200.00 to cover any losses, before the insurance company pays the rest of the claim. Deductible’s can range from \$100- \$5,000 or more. The higher the deductible the lower the insurance premium. By increasing your current \$200.00 deductible to a \$1000.00 deductible, you might save 20 to 30 percent on your premiums. You may not have to switch companies to accomplish this feat. Your present company can usually oblige you by amending your current policy and reducing your premium.

The Old Man cautioned, “always check your policy ; some insurance companies may have a separate deductible in areas prone to similar damage claims , like if you live near the coast in the East, you may have a separate windstorm deductible or if you live anywhere near the San Andreas fault line in California, you may have a separate earthquake deductible. Translation: Some insurance policies have two deductibles; one for regular claims and another one for specific claims, like wind damage in the east or earthquake damage in the west.

The Old Man reassured me, “don’t worry about the size of your deductible”, if tragedy ever struck you can usually recover your deductible expense by hiring your own adjuster, a **public**

adjuster, to negotiate on your behalf (for a fee) with your insurance company. The old man said you should always use a public adjuster on any medium – large insurance claim.

- 3) **Do Not Overinsure**- do not include the value of land in deciding how much homeowners insurance to buy, otherwise you will pay a higher premium than you should. The price you paid for the house and the price it would take to rebuild the house in the event of a catastrophe are not the same. For example, if you bought a 3000 square foot house for \$800,000 , and the average cost to rebuild in the area is \$125.00 per square foot, you would only need coverage of \$375,000 ($125 \times 3000 = 375$) to rebuild structure not \$800,000. The expensive land that this house sits on isn't at risk from windstorm, fire, theft, lightning and any of the other perils covered in your homeowner's policy.

The old man warned, “ don't let your mortgage company pressure you into getting more insurance on your property than you need “. In the above example if you had a \$600,000 mortgage on the property, you don't need to get a \$600,000 insurance policy to cover the lender's money, the cost of rebuilding the structure hasn't changed it would still cost the same \$375,000 to completely rebuild the house and protect the lender's collateral. You would only need to pay the premium on a \$375,000 insurance policy to adequately protect this \$600,000 mortgage loan.

- 4) **Package Insurance for a Discount**-

Some companies will lower your overall insurance bill by 5-15 % if you “package” your insurance by buying two or more policies from them. For example, if you had your homeowner's and auto policy with the same company, this “packaged deal “could net you a reduction in your insurance premium.

The Old Man cautioned, “Do your homework”, make sure this combined price is lower than buying the different coverages from different companies.

- 5) **Maintain Good Credit**- some insurers will penalize you with higher insurance premiums if you have bad credit. Translation: Good credit is the key to low insurance premiums. To protect your credit rating you should a) pay your bills on time b) don't obtain needless credit c) keep your credit balances as low as possible and d) check your credit report annually. If you find any misinformation, errors or discrepancies on your credit report, which can adversely affect your credit rating, and erroneously raise your insurance premiums, you should promptly correct your credit, to avoid overpaying . If derogatory information cannot be corrected , because it really happened, you are entitled by law to add a statement of up to 100 words to your official credit report to explain the circumstances of your delinquent credit, like loss of job, death, divorce, sickness, etc...

*As a side note the Old man recommended obtaining a 1-2 million dollar umbrella policy for an even greater layer of protection from liability exposure.

The old man said the ultimate goal of increasing your positive cash flow is the creation of the **Pension Walker**. . A Pension Walker is a tenant that pays for your retirement, in effect being your walking & talking pension, by giving you maximum positive cash flow dollars by living in your paid off/free & clear “cash cow”. The Pension Walker is not to be confused with a regular tenant. You might go through 10 or 15 tenants before you pay off rental and

arrive at your first **Pension Walker**. The amount of money that the Pension walker puts in your pocket each and every month commands your instant respect and admiration. A regular tenant helps you pay your bills by putting hundreds a month in your wallet, pension walkers can change your life by giving you the bankroll you need to enjoy a whole new style of living, namely the regal lifestyle of a King of the Middle Class The collective money generated by pension walker’s every month is the hidden wealth created by the old man’s investing system. The old man hid that wealth in plain sight; everyone knew he had rentals and made money with tenants, few people knew his rentals were paid off and he had pension walkers that were putting five figures a month in his coffers. The Old man was silently rich.

The Pension Walker is the retirement vehicle of choice for the self-employed. The self-employed business owner, who does not have matching 401 k contributions from a corporate giant like regular employees, can legally bury their money in real estate creating pension walkers that can outperform some of the better 401 k ‘s. The self employed who do not have the luxury of a fat pension from a fortune 1000 company can no longer sit idle and wait for the government to subsidize their retirement through social security payments. The old man said, “Do the research”, you could never retire and live comfortably on social security payments alone and furthermore social security could be bankrupt by the time you reach entitlement age. I took the liberty of researching this fact in 2003, 6 years after his passing and I was astounded to discover after 30 or so years of hard work the average dole out from Uncle Sam was only \$895 per month. The old man had a valid point. You could not possibly survive on social security alone, you either needed to get a new job after you retired from your old job or you needed supplemental income from another source like a corporate pension or dare I say the highly touted **Pension Walker**. **The old man said, its your call “ you can retire like the average American on \$895 per month social security or you can invest in real estate and retire like a self employed king with a stable of pension walkers putting \$2-10,000 per month in your pocket.**

<i>Estimated Average Monthly Social Security Benefits Payable in January 2003:</i>	Before 1.4% COLA	After 1.4% COLA
All Retired Workers	\$ 882	\$895
Aged Couple, Both Receiving Benefits	\$1,463	\$1,483
Widowed Mother and Two Children	\$1,812	\$1,838
Aged Widow(er) Alone	\$ 850	\$ 862
Disabled Worker, Spouse and One or More Children	\$1,376	\$1,395
All Disabled Workers	\$ 822	\$ 833

www.ssa.gov

The Old Man said if you are not looking to retire the pension walker is the greatest part-time job in the world. Do the Math son! the numbers don’t lie. Let’s say you invested wisely and you have two paid off rental properties generating a \$1000 per property positive cash flow. That’s \$2,000 per month. Translation; You have two pension walker’s putting a grand a month each in your pocket. How many hours per week do you have to work to get that \$2,000 per month? Lets see:

Average Time the Old Man Spent as Landlord of 2 “Cash Cows”:

- A. Hire Handyman - (avg. 1-2 hours for estimates)
- B. Buy supplies for fix up - (avg. 2 hours @ Home Depot)
- C. Monitor Handyman- (avg. 2-8 hrs. - periodic inspections)
- D. Place classified ad for rental - (avg.- 1 hour- ½ hr to design ad, ½ hr phone call to place ad)
- E. Show Unit to prospective tenants- (avg. 0 hrs – Save the time & let a professional realtor do it for you. It’s FREE!)
- F. Selecting tenants
 - 1.Tenant application filled out- (avg. 0 hr-Save the time; Realtors do it for you for FREE!)
 - 2.Run credit report- (avg. 0 hr-Save the time; Realtors do it for you for FREE!)
 - 3.Run criminal check- (avg. 0 hr-Save the time; Realtors do it for you for FREE!)
 - 4.Verify income- (avg. ½ hr – call employer)
 - 5.Fill out lease / collect money- (avg. 1-2 hrs- in person)
- G. Pay bills on property- (avg. 1hour- ½ hr to pay bills, ½ hr for deposits)
- H. Settle tenant disputes- (avg. 2 hrs. - 1 hr drive time, 1 hr resolve time)
- I. Evict non-paying tenants- (avg. 0 hrs. - The old man never wasted his time going to court; he always hired an attorney to do it for him.)

The old man said on average he probably put in 10 hours per month per rental unit. That’s 20 hours of work per month for \$2000.00. That’s 240 hours of work per year. (20 hours X 12 months= 240 hours per year). That’s about 5 hours per week (240 hours divided by 52 weeks = 4.62 average hours per week worked on rentals) Now lets do the math; \$2000 X 12 months = \$24,000 for the year divided by 52 weeks = \$461.54 per week. This \$461.54 per week divided by the # of hours worked for the week (5) gives you a grand total of \$92.31 per hour. The Old Man boastfully proclaimed, the pension walker is the greatest part-time job in the world it pays \$92.31 per hour regardless of your education level, work experience or technical skills. The Old man said the biggest perk of this extraordinary part-time job is that once your unit is fully rented you punch a time clock once a month, not twice daily like a regular job.

Now let’s wrap up what we learned. What makes real estate a powerful investment?

- 1) **Forced Equity**- the natural by product of amortization
- 2) **Market Equity**- the increased value created by the laws of supply & demand
- 3) **Tax write offs**- pay less taxes with attractive real estate deductions & loopholes
- 4) **Positive Cash Flow**- the steady stream of passive income generated by Pension Walkers

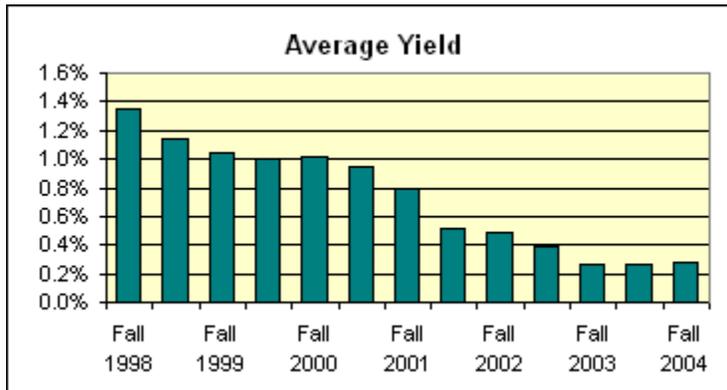
The Old man said , now let’s prove it **Talk is Cheap, Results Speak** , lets crunch the numbers and prove the financial worthiness of the rental property investment. Let’s say you had \$75,000 to invest over a 10-year period, which investment vehicle would yield you the highest return on your money? The Old man said , do the research son , show the average Joe or Jane what happens to \$75,000 when you invest it in different financial products. The common choices for the average investor are :

- 1) Regular interest bearing savings account
- 2) Certificates of Deposit/ Bonds
- 3) Mutual fund
- 4) Stocks
- 5) Real estate

Your mission son is to research these investment vehicles and figure out which one, on average will make you the most money over a 10 year consecutive period of time. I do not want you to blindly trust me on the merits of the rental property investment, I raised you better than that. I want you to prove it to yourself, so that you can confidently and safely park your hard earned dollars where the old man did: rental properties. I love you son , and I wouldn’t steer you wrong but you owe it yourself and your growing family’s future to place your money in the investment that will yield you the most money . The

only way you are going to figure that out is by doing your homework and compiling the data you need to make this all-important decision. Now GO FIGURE !

I embarked on this fact finding mission immediately after his death, but updated the results for this publication in late 2005. I started with the most obvious place that middle class people know of to place their money; the regular interest bearing savings account. According to bankrate.com the average yield in interest bearing accounts is a whopping .28 % (that's less than 1/3 of 1 %).



www.bankrate.com

For illustration purposes I elected to give myself and other investors a much higher than average return on the money; a respectable 2 % Personally, my own account at a major bank pays .40 % if you have less than 10,000 in it, 2.5 % if you maintain 10,000 or better. Translation: unless you have an extra \$10,000 you can park in a bank indefinitely you will be penalized with a paltry return on your money. A tall order for the average middle class investor struggling to make ends meet.

Regular Interest bearing savings account

@ 2%

Year 1- 75,000 - 1500 = 76,500

Year 2- 76,500 - 1530 = 78,030

Year 3 - 78,030- 1560.60 = 79,590.60

Year 4- 79,590.60- 1591.81 = 81,182.41

Year 5- 81,182.41- 1623.65 = 82,806.06

Year 6- 82,806.06- 1656.12 = 84,462.18

Year 7- 84,462.18- 1689.24 = 86,151.42

Year 8- 86,151.42- 1723.03 = 87,874.45

Year 9- 87,874.45- 1757.49 = 89,631.94

Year 10- 89,631.94- 1792.64 = 91,424.58

Total Profit 10 Yrs. = \$16,424.58 (91,424.58 - 75,000)

Monthly Profit = \$136.87

(16,424.58 divided by 120)

NET MONTHLY PRE TAX INCOME = \$136.87 (Pre tax)

\$ 136.87 (Pre tax)

Rate of return for the interest bearing savings account

Calculated as (value now - value at time of purchase) / (value at time of purchase)

Regular Savings account

Value Now- \$91,424.58

Value at time of purchase- 75,000

\$91,424.58 -75,000= \$16,424.58

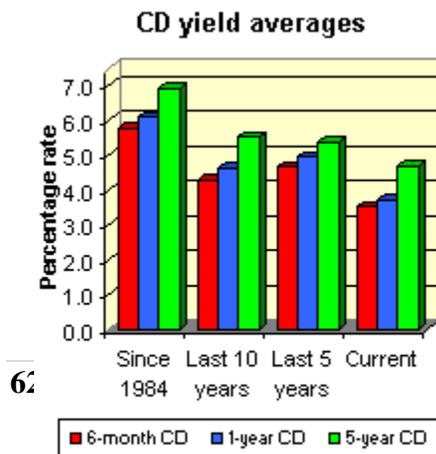
16,424.58 divided by 75,000= **10 Year Return 22 %**

As the figures clearly show if I took my \$75,000 and conveniently parked it in a savings account for 10 years I would have \$ 91,424.58, a gain of \$ 16,424.58 or an average monthly gain of \$136.87 for 120 months. In 10 years I have increased the value of my money by a measly 22 %. The numbers don't lie, there is only one group of investors that I know that fares worse than this; the "mattress money crowd". The people in society that don't trust banks and the protection of the FDIC, and chose not to invest there money , opting to hide there cash in a wall safe or some other proverbial "mattress" location. This is the same crowd that abhors credit and usually pays cash for everything, even depreciating assets like cars, boats and computers. This group earns a dismal 0 % return on their money after 10 years of non investing. If you factor in inflation this group actually has a below zero return. The \$75,000 they started with 10 years ago actually loses value over time due to the rising cost of living expenses. What cost \$1.00 10 years ago, might cost \$1.25 or more today. This group brags about how much interest they are saving by not using credit cards, yet they are oblivious to how much money they are losing by not properly investing their hoarded money. They are one fire or robbery away from poverty.

The second investment vehicles I focused my energy on was certificates of deposit and bonds. According to bankrate.com a certificate of deposit is:

" A time deposit, FDIC insured to \$100,000 per person, with a fixed maturity date, usually from three months to five years. It usually pays higher interest than a savings account and a penalty is charged for withdrawing funds before the maturity date."

If I had \$75,000 to invest over 10 years I would acquire a \$75,000 5year certificate of deposit and upon maturity roll it over into another 5-year certificate of deposit, completing my 10-year investment cycle. According to bankrate.com the average yield on a 5-year certificate of deposit is a little less than 7 %.



According to Webster's dictionary a bond is :

“ an interest- bearing certificate issued by a government or business promising to pay the holder a specified sum on a specified date.”

Basically, you have two choices where to place your hard earned dollars in the bond market , the government or corporations. According to bankrate.com “ corporate bonds are the riskiest of the fixed income securities because only the individual corporation backs them and companies are much more likely to have serious financial problems.” And conversely according to the same source , bankrate.com, “U.S. savings bonds are very safe: they are backed by the full faith and credit of the U.S. government.” Naturally I would opt for the safety of patriotism over the higher risks associated with corporate greed and park my money with Uncle Sam. The government is less likely than a corporation to go bankrupt so I would proudly invest in government bonds. There are basically two types of government bonds you can invest in, Series I and Series EE.

You wont be able to buy these bonds all in the same year, there are annual limitations on how much bonds can be purchased . On the Series I bonds the annual purchase limit per social security number is \$30,000 per year. The annual purchase limit per social security number on Series EE bonds is \$15,000. You can invest \$45,000 one year and \$30,000 the next year to complete your \$75,000 investment. According to the bureau of public debt: Series I bonds pay 6.73 % per year and Series EE pay 3.20 % per year.

Current Rates:
(through Apr. 2006)
I Bonds = 6.73%
EE Bonds = 3.20% FIXED
New rates will be posted on May 1, 2006.
HH Bonds = 1.5%

Source- www.publicdebt.treas.gov

For comparison purposes I chose to give myself a little better than average return on my government bonds investment a 7 % return to be exact, the same return I could receive on certificates of deposit.

Certificates of Deposit / Government bonds

@7%

Year 1- 75,000- 5250 = 80,250
Year 2- 80,250- 5617.50=85,867.50
Year 3- 85,867.50-6010.73=91,878.23
Year 4- 91,878.23-6431.48= 98,309.71
Year 5- 98,309.71-6881.68=105,191.39
Year 6- 105,191.39-7363.40 =112,554.79
Year 7- 112,554.79-7878.84= 120,433.63
Year 8- 120,433.63-8430.35=128,863.98
Year 9- 128,863.98-9020.48=137,884.46
Year 10- 137,884.46-9651.91= 147,536.37

Total Profit 10 Yrs. = \$72,536.37 (147,536.37– 75,000)
Monthly Profit = \$604.47
(72,536.37 divided by 120)
NET MONTHLY PRE TAX INCOME = \$604.47(Pre tax)
\$ 604.47 (Pre tax)

Rate of return for Certificates of deposit/Government bonds

Calculated as (value now - value at time of purchase) / (value at time of purchase)

Certificate of deposit/Government bonds

Value Now- \$ 147,536.37

Value at time of purchase- 75,000

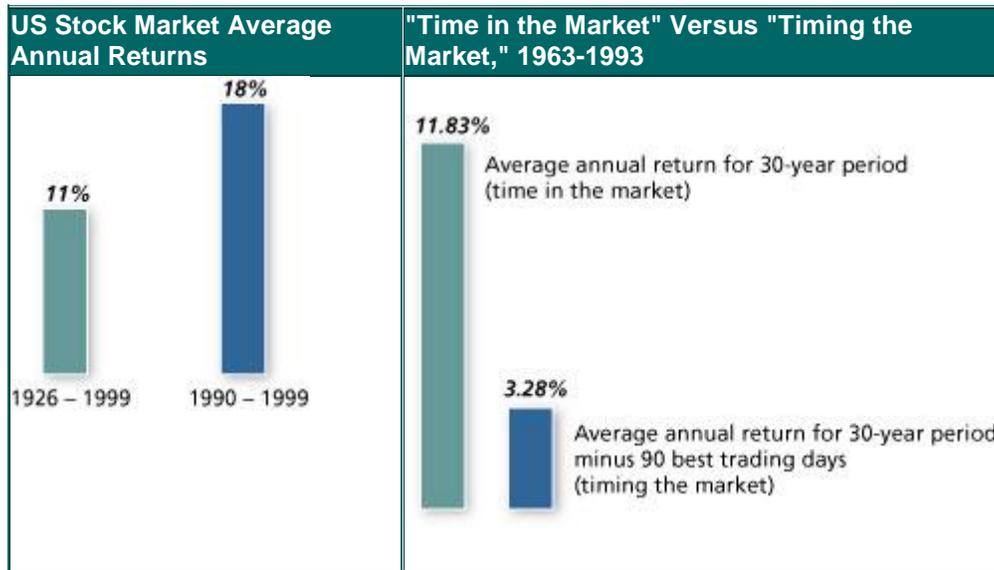
\$147,536.37 -75,000= \$72,536.37

72,536.37 divided by 75,000= **10 Year Return 96.7 %**

As the figures clearly show if I took my \$75,000 and placed it in certificates of deposits or government bonds , for 10 years I would have \$147,536.37, a gain of \$72,536.37 or an average monthly gain of \$604.47 for 120 months. In 10 years I have increased the value of my money by 96.7 % . Translation: in 10 years you almost doubled the value of your money .

The next investment vehicle I zeroed in on was mutual funds. Quite simply, a mutual fund is an investment company that pools money from many individual investors to purchase stocks, bonds or other types of investments. Choosing which type of mutual fund to invest in is a daunting task for the average unsophisticated middle class investor. According to David Harrell of Morningstar.com, “It’s gotten to the point where it ‘s overwhelming even for an experienced investor .” Harrell goes on to say, “ A common mistake people make when choosing funds is to look at lists of funds with the biggest returns last year- and then buy them.” Harrell states “...what’s done well recently could easily have the lowest return in the near future; primarily because of the cyclical nature of the stock market.” According to www.fool.com, “ Almost all actively managed equity mutual funds over time lose to the market averages. And those funds that do beat the market’s return typically do so for only a very short period of time, and then quickly reverse course.” The lesson to be learned here is that past performance of a mutual fund is in no indication of it’s future success. The best advice I found on mutual funds was cut out the expense of the middleman (the proactive manager)and according to, www.fool.com , “Buy an Index fund “.According to www.investopedia.com, “Index funds are simply mutual funds based on an index so as to mirror it’s performance.” As per the Motley fool, “ A index fund simply seeks to match “the market” by buying representative amounts of each stock in the index, rather than paying a manager to make bets on individual stocks, sectors , or investment strategies. Index funds do not even attempt to beat the equities market, they simply seek to come as close as possible to equaling it. The key to the unquestioned superiority of index funds is their extremely low expenses- they charge very low fees for providing the market’s returns.” Naturally I elected to place my hypothetical \$75,000 investment in mutual funds in an index fund.

Now I had to figure out what was the average return I could realistically expect from investing in an index fund. According to www.fool.com , “On the whole . the average mutual fund returns approximately 2 % less per year to it’s shareholders than does the stock market in general. The stock market ‘s historical returns are roughly 11 % per year...” (I confirmed the validity of the stock market’s historical 11 % average return on a website called www.finfacts.com ; see chart), so a 9 % return looked like a safe number to use for a regular mutual fund and 11 % seemed like the right number to use for an index fund that mirrored the activity of the stock market. But before I used this number as my benchmark, I wanted to prove to myself that an index fund could actually outperform a regular mutual fund. I found that proof in a book written by Burton Malkiel, called “A Random Walk Down Wall Street”. His book begins by comparing a \$10,000 investment in the S&P 500 Index to a \$10,000 investment in an average actively managed mutual fund. The time period was the beginning of 1969 through June 30, 1998. The results were indisputable, the index investor was ahead nearly \$140,000; the original \$10,000 increased 31 times to \$311,000 while the regular actively managed mutual fund investor ended up with only \$171,950. Now I was sold, my hard earned dollars would migrate from my pocket to the S&P Index fund (translation: Standard & Poors 500 – the stocks of 500 leading companies in leading industries) . According to www.investopedia.com , “historically, the return of the S&P 500 has been around 10-11 %...”



Source: Ibbotson Associates
www.finfacts.com

Source: University of Michigan

I opted for a little better than market average return and gave myself a pay raise and upped my 11 % return to a more respectable 12 % . Now I had to crunch my numbers and GO FIGURE .

Index Fund

@ 12 %

Year 1- 75,000-9000= 84,000
Year 2- 84,000- 10,080= 94,080
Year 3- 94,080-11,290= 105,370
Year 4- 105,370-12,644= 118,014
Year 5- 118,014-14,162= 132,176
Year 6- 132,176-15,861= 148,037
Year 7-148,037-17,764= 165,801
Year 8- 165,801-19,896= 185,697
Year 9- 185,697-22,283=207,980
Year 10- 207,980-24,958=232,938

Total Profit 10 yrs. = \$157,938 (232,938-75,000)

Monthly Profit = 1316.15

(157,938 divided by 120)

Net Monthly Pre tax Income = 1316.15

\$ 1316.15

Rate of return for Index Fund

Calculated as (value now - value at time of purchase) / (value at time of purchase)

Index fund

Value Now- \$ 232,938

Value at time of purchase- 75,000

\$232,938 -75,000= \$157,938

157,938 divided by 75,000= **10 Year Return 211 %**

As the figures clearly show if I took my \$75,000 and parked it in a index fund for 10 years I would have \$232,938, a gain of \$157,938 or an average monthly gain of \$1316.15 for 120 months. In 10 years I have increased the value of my money by 211 %.

I had a head start on the next stage of my exploratory mission ; the stock market. I already confirmed from my research on mutual funds what return to typically expect from this investment vehicle ; 11 % . The real question was, do I chose individual stocks or do I stick with the same logic as mutual funds and invest in an index fund like the venerable S&P 500 Index fund. Translation; Do I want to have \$311,000 in my pocket after 29 years of steady investing or did I want to take my chances at beating the market and wind up with \$171,950 after 29 years of researching and investing in various companies (the commissions alone would run into the tens of thousands). Well, Momma didn't raise a dummy, this seemed like a no brainer decision I would place my hard earned \$75,000 in an historically proven winner the coveted index fund. But before I committed myself to this line of thinking I wanted to prove to myself

how difficult picking winning stocks really was. The answer to this question was provided by Piper Jaffray, a brokerage and investment banking firm with five offices in northern California, they conducted a stock picking contest in 1997 in conjunction with the San Francisco business Times. The contest was simple. Each contestant started the game with a hypothetical \$100,000 bankroll to invest in the stocks of their choice, whichever investor had the greatest return on their money in 6 months won the game. To make the contest a little more interesting celebrity contestants such as radio DJ Steven Seaweed, San Francisco Supervisor Barbara Kaufman and Zura the gorilla (a real gorilla) from the San Francisco Zoo were entered into the competition. The results were astounding. The last place finisher was Karyn DiGiorgio of San Francisco, who lost almost 42 % of the value of her hypothetical stock portfolio in six months. The big winner was a neophyte investor from Berkeley named Jocelyn Krygier, who posted an impressive 45 % gain in value over the same six months. The big surprise came with the celebrity contestants, Zura a primate with gorilla investing skills came in toward the middle of the pack and posted a 9 % gain topping the other two celebrity investors, DJ Steven Seaweed (a 4 % gain) and Barbara Kaufman (a 17 % loss). I guess picking winning stocks isn't as easy as everyone thinks it is and since I don't own a gorilla I guess I'll stick with the original gameplan and invest in an index fund.

So obviously my research on investing in stocks is complete, all the previous calculations concerning mutual funds are fully applicable to the stock investment. The Index fund would be my choice for investing in either one of these financial vehicles. I now proved to myself with facts and figures how much to realistically expect from the most common investment choices presented to the average middle class investor. I now wanted to prove what my old man already knew ; that real estate and the power of rentals could yield an even higher return than any other conventional financial products.

Unlike the other investment vehicles, where I gave myself a little better than average return, I opted to downplay the figures on real estate and be ultra conservative in my calculations. I figured if this investment vehicle (rental property) was as good as the old man said it was it wouldn't matter. I started my foray into real estate investing by taking my \$75,000 and buying a rental property. Here's how it went down:

Purchase Price = \$260,000
Down Payment = \$52,000 (20% Down) No PMI
Closing costs = \$ 13,000
Cash Reserve = \$ 10,000 (repairs/eviction etc..)
Total \$ Invested = **\$75,000**(Down payment & Closing costs & Cash reserve)

Mortgage (P&I)= \$208k@ 7%= \$1384
Property Taxes (estimated 6000)= 500
Homeowners Ins (estimated 600)= 50

Total monthly payment = \$1934

House- 3-4 Br Ranch Full basement
Rental Value = estimated @ 2500 month

I used \$52,000 of my \$75,000 investment as a down payment, I allocated \$10,000 as a cash reserve to offset any unforeseen expense like an emergency repair or eviction . I used the remaining investment dollars (\$13,000) to cover the closing costs associated with buying the rental. I now owned an investment vehicle called a rental property. Now I had to figure out what was the average return I could realistically expect from investing in my old man's favorite investing vehicle the revered rental property. I had to take those four reasons the old man cited previously 1) forced equity, 2) market equity, 3) tax

write-offs & 4) positive cash flow and plug them into the rental property investment to calculate an average return on my money. I had to crunch the numbers to prove to myself the financial worthiness of this investing product.

CRUNCH YOUR NUMBERS

- **“Forced Equity”**- Principal Balance Reduction
Month-by-Month analysis – 10 year
208,000 @7% 30 yr. \$1383.83 (round off 1384)
Year 1 = 208,000 to 205,887 = \$2113
Year 2= 205,887 to 203,621 = \$2266
Year 3 = 203,621 to 201,192 = \$2429
Year 4 = 201,192 to 198,587 = \$2605
Year 5 = 198,587 to 195,794= \$2793
Year 6 = 195,794 to 192,798= \$2996
Year 7= 192,798 to 189,587= \$3211
Year 8 = 189,587 to 186,143= \$3444
Year 9 = 186,143 to 182,450=\$3693
Year 10= 182,450 to 178,490= \$3960

Total 10 years = \$29,510

29,510 DIVIDED BY 120 MONTHS= 245.92 PER MONTH

- **“Market Equity”** – Appreciation
HISTORICALLY NEW YORK HAS RISEN AT 10.23% PER YEAR SINCE 1990 - NATIONALLY THE ENTIRE USA HAS RISEN AT 7.71% PER YEAR. FIVE % PER YEAR IS A VERY CONSERVATIVE ESTIMATE.

Assuming only a **5%** Appreciation Rate Per Year

YR 1- 260,000 – 5%- 13,000- 273,000
YR 2- 273,000- 5%- 13,650-286,650
YR 3- 286,650- 5%- 14,332 – 300,982
YR 4- 300,982- 5%- 15,049- 316,031
YR 5- 316,031-5% - 15,801- 331,832
YR 6- 331,832- 5%- 16,592- 348,424
YR 7- 348,424- 5%- 17,421- 365,845
YR 8- 365,845- 5%- 18,292- 384,137
YR 9- 384,137- 5%- 19,207- 403,344
YR 10- 403,344-5%- 20,167- 423,511

TOTAL APPRECIATION 10 YRS = \$163,511

Bear in mind this gain will only be activated by selling the rental or cashing out tax-free by refinancing.(God bless your wonderful tenants)

163,511 DIVIDED BY 120 MONTHS= 1362.59 PER MONTH

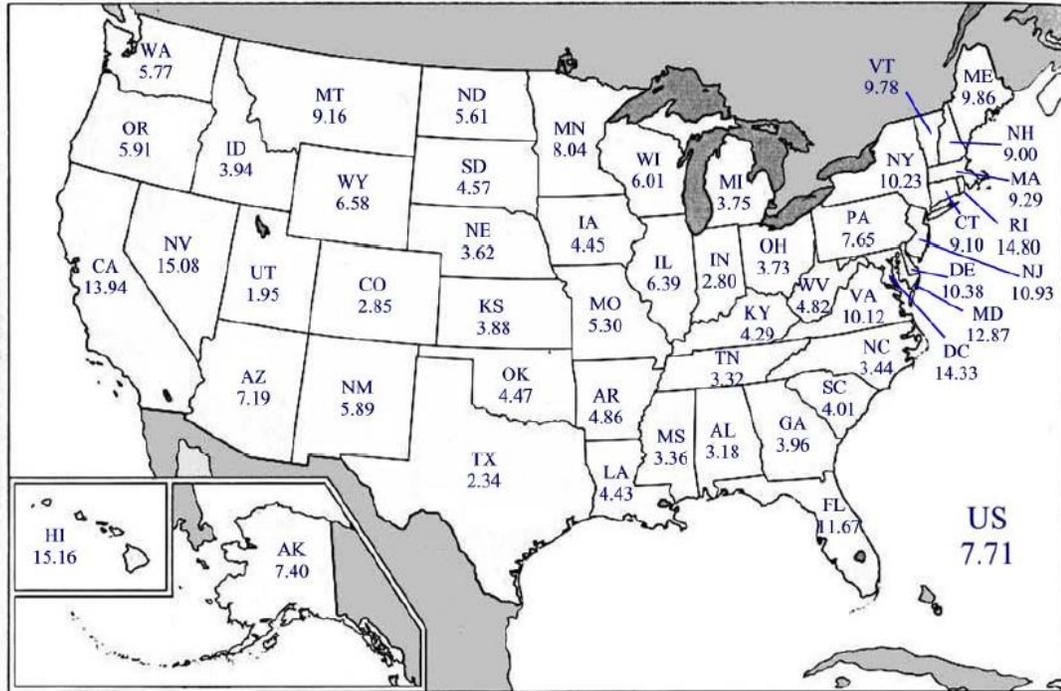
HISTORICALLY NEW YORK REAL ESTATE HAS RISEN 398.79 % SINCE 1980. IF YOU BOUGHT A HOUSE IN 1980 FOR \$100,000 IT WOULD BE WORTH ALMOST \$400,000 NOW

Here’s the proof for my conservative appreciation rate calculations:

One Year Change in House Prices

First Quarter 2003 to First Quarter 2004

Average U.S. Annual Appreciation = 7.71



Source:



Office of Federal Housing Enterprise Oversight (OFHEO)
1700 G Street, NW 4th Floor
Washington, DC 20552
Phone: 202-414-3800
Fax: 202-414-3823

Tim Larkin
King of the Middle Cass
www.rkrynys.com

OFHEO HOUSE PRICE HISTORY FOR USA

Quarter	House Price Quarterly Appreciation (%)	House Price Quarterly Appreciation Annualized (%)	House Price Appreciation From Same Quarter One Year Earlier (%)
1990Q1	0.41%	1.65%	5.05%
1990Q2	-0.04%	-0.17%	3.62%
1990Q3	0.31%	1.23%	1.63%
1990Q4	-0.47%	-1.87%	0.21%
1991Q1	0.76%	3.03%	0.55%
1991Q2	0.42%	1.68%	1.02%
1991Q3	0.00%	-0.01%	0.71%
1991Q4	1.34%	5.37%	2.53%
1992Q1	0.67%	2.67%	2.44%
1992Q2	-0.23%	-0.92%	1.78%
1992Q3	1.00%	4.00%	2.80%
1992Q4	0.41%	1.65%	1.86%
1993Q1	-0.16%	-0.66%	1.02%
1993Q2	0.82%	3.29%	2.08%
1993Q3	0.59%	2.35%	1.67%
1993Q4	0.76%	3.04%	2.02%
1994Q1	0.47%	1.86%	2.66%
1994Q2	0.31%	1.23%	2.14%
1994Q3	0.25%	1.00%	1.79%
1994Q4	-0.25%	-0.99%	0.77%
1995Q1	0.36%	1.43%	0.67%
1995Q2	1.73%	6.92%	2.09%
1995Q3	1.55%	6.19%	3.42%
1995Q4	0.80%	3.18%	4.50%
1996Q1	1.20%	4.81%	5.38%
1996Q2	0.10%	0.39%	3.69%
1996Q3	0.37%	1.49%	2.49%
1996Q4	0.88%	3.53%	2.58%
1997Q1	0.90%	3.60%	2.27%
1997Q2	0.81%	3.26%	3.00%
1997Q3	1.48%	5.91%	4.14%
1997Q4	1.33%	5.31%	4.60%
1998Q1	1.52%	6.07%	5.24%
1998Q2	0.81%	3.23%	5.23%
1998Q3	1.37%	5.47%	5.11%
1998Q4	1.19%	4.76%	4.97%
1999Q1	1.06%	4.22%	4.49%
1999Q2	1.38%	5.52%	5.09%
1999Q3	1.60%	6.42%	5.33%
1999Q4	1.15%	4.61%	5.29%
2000Q1	2.09%	8.34%	6.37%
2000Q2	1.73%	6.92%	6.73%
2000Q3	1.96%	7.85%	7.11%
2000Q4	1.64%	6.57%	7.63%
2001Q1	2.57%	10.27%	8.14%
2001Q2	1.82%	7.30%	8.24%
2001Q3	1.67%	6.66%	7.92%
2001Q4	1.28%	5.13%	7.54%
2002Q1	1.69%	6.77%	6.62%
2002Q2	1.92%	7.70%	6.72%
2002Q3	2.18%	8.71%	7.26%
2002Q4	1.65%	6.58%	7.65%
2003Q1	1.35%	5.40%	7.29%
2003Q2	1.21%	4.85%	6.54%
2003Q3	1.64%	6.56%	5.98%
2003Q4	3.71%	14.85%	8.13%
2004Q1	0.96%	3.84%	7.71%

House Price Appreciation by State Percent Change in House Prices *Period Ended March 31, 2004*

State	* 1-Yr.	1-Yr	Qtr.	5-Yr.	Since 1980
Hawaii, (HI)	1	15.16	3.89	43.98	236.60
Nevada, (NV)	2	15.08	4.18	40.37	160.79
Rhode Island, (RI)	3	14.80	1.26	80.24	361.36
District of Columbia, (DC)	4	14.33	3.20	92.96	302.84
California, (CA)	5	13.94	2.11	76.97	314.95
Maryland, (MD)	6	12.87	1.84	52.26	245.90
Florida, (FL)	7	11.67	2.07	55.42	195.57
New Jersey, (NJ)	8	10.93	0.63	61.82	315.63
Delaware, (DE)	9	10.38	1.60	44.61	265.53
New York, (NY)	10	10.23	0.61	61.36	398.79
Virginia, (VA)	11	10.12	1.66	48.66	223.63
Maine, (ME)	12	9.86	1.01	56.68	302.32
Vermont, (VT)	13	9.78	-0.68	43.84	238.71
Massachusetts, (MA)	14	9.29	1.16	75.50	516.30
Montana, (MT)	15	9.16	1.29	32.41	170.25
Connecticut, (CT)	16	9.10	0.90	50.49	273.03
New Hampshire, (NH)	17	9.00	0.55	71.33	307.20
Minnesota, (MN)	18	8.04	0.40	56.18	216.43
United States **	.	7.71	0.96	41.73	209.60
Pennsylvania, (PA)	19	7.65	0.67	32.86	206.89
Alaska, (AK)	20	7.40	-0.49	24.80	103.72
Arizona, (AZ)	21	7.19	1.12	34.78	152.85
Wyoming, (WY)	22	6.58	0.90	31.40	93.22
Illinois, (IL)	23	6.39	0.71	33.54	201.72
Wisconsin, (WI)	24	6.01	0.27	29.86	172.41
Oregon, (OR)	25	5.91	0.57	24.72	202.92

* Note: Rankings based on annual percentage change.

** Note: United States figures based on weighted division average.

House Price Appreciation by State Percent Change in House Prices *Period Ended March 31, 2004*

State	* 1-Yr.	1-Yr	Qtr.	5-Yr.	Since 1980
New Mexico, (NM)	26	5.89	0.69	19.51	138.92
Washington, (WA)	27	5.77	1.02	29.43	228.77
North Dakota, (ND)	28	5.61	-0.39	21.84	96.35
Missouri, (MO)	29	5.30	0.40	30.82	156.10
Arkansas, (AR)	30	4.86	0.92	20.70	116.07
West Virginia, (WV)	31	4.82	0.57	20.68	100.06
South Dakota, (SD)	32	4.57	-0.54	24.46	135.12
Oklahoma, (OK)	33	4.47	1.05	24.00	73.91
Iowa, (IA)	34	4.45	-0.07	22.90	120.76
Louisiana, (LA)	35	4.43	0.27	24.38	92.11
Kentucky, (KY)	36	4.29	0.57	22.77	157.52
South Carolina, (SC)	37	4.01	0.84	24.81	161.67
Georgia, (GA)	38	3.96	1.11	30.25	184.12
Idaho, (ID)	39	3.94	0.61	18.61	136.88
Kansas, (KS)	40	3.88	0.25	25.67	114.68
Michigan, (MI)	41	3.75	0.27	29.28	202.55
Ohio, (OH)	42	3.73	0.35	21.28	154.63
Nebraska, (NE)	43	3.62	-0.01	19.43	129.16
North Carolina, (NC)	44	3.44	0.81	21.14	177.93
Mississippi, (MS)	45	3.36	0.43	19.15	110.86
Tennessee, (TN)	46	3.32	0.35	18.38	150.87
Alabama, (AL)	47	3.18	0.80	19.67	134.49
Colorado, (CO)	48	2.85	0.42	40.54	223.93
Indiana, (IN)	49	2.80	0.10	18.01	137.09
Texas, (TX)	50	2.34	0.20	26.03	88.60
Utah, (UT)	51	1.95	0.77	9.98	162.56

* Note: Rankings based on annual percentage change.

** Note: United States figures based on weighted division average.

- **TAX WRITE –OFFS**

Average tax savings per year could be 4-5000 a year.(very conservative-a good CPA could probably double or triple this number)

Interest on mortgage

Property taxes

Homeowners ins.

Repairs

Maintenance

Depreciation

Advertising/mileage/legal fees/ etc....

4000 times 10 years= \$40,000

40,000 divided by 120 months = **333.33 per month**

- **Positive Cash Flow-** PITI= 1934
 Rent Roll = 2500

2500 minus 1934= \$566 month

PCF = \$566 Per Month (God Bless America)

(Your P&I is a constant fixed number; the T for property taxes usually goes up yr after yr and the I for homeowners insurance can go up as well. For our illustration we will keep rent as a constant ; bear in mind rent is normally adjusted upward to reflect any increase in prop tax or insurance)

Year 1 = 566 times 10 months= 5660 (**2mths per year vacancy factor**)(566 × 12=6792)

Year 2= 5660

Year 3=5660

Year 4=5660

Year 5=5660

Year 6=5660

Year 7= 5660

Year 8=5660

Year 9=5660

Year 10=5660

Total 10 years = 56,600

56,600 Divided by 120 months = **472 NET PCF PER MTH**

I was very conservative on the PCF calculations, I assumed 2 months per year vacancy and I did not adjust the rent for inflation.

Rental Property investment

Real Estate Breakdown 10 year

FE= Forced Equity | ME= Market Equity | TW=Tax Write-offs | PCF= Positive Cash Flow

<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 1</td><td>FE</td><td>2113</td></tr> <tr><td></td><td>ME</td><td>13,000</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>24,773</u></td></tr> </table>	YEAR 1	FE	2113		ME	13,000		TW	4000		PCF	5660		<u>TOTAL</u>	<u>24,773</u>	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 2</td><td>FE</td><td>2266</td></tr> <tr><td></td><td>ME</td><td>13,650</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>25,576</u></td></tr> </table>	YEAR 2	FE	2266		ME	13,650		TW	4000		PCF	5660		<u>TOTAL</u>	<u>25,576</u>
YEAR 1	FE	2113																													
	ME	13,000																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>24,773</u>																													
YEAR 2	FE	2266																													
	ME	13,650																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>25,576</u>																													
<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 3</td><td>FE</td><td>2429</td></tr> <tr><td></td><td>ME</td><td>14,332</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>26,421</u></td></tr> </table>	YEAR 3	FE	2429		ME	14,332		TW	4000		PCF	5660		<u>TOTAL</u>	<u>26,421</u>	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 4</td><td>FE</td><td>2605</td></tr> <tr><td></td><td>ME</td><td>15,049</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>27,314</u></td></tr> </table>	YEAR 4	FE	2605		ME	15,049		TW	4000		PCF	5660		<u>TOTAL</u>	<u>27,314</u>
YEAR 3	FE	2429																													
	ME	14,332																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>26,421</u>																													
YEAR 4	FE	2605																													
	ME	15,049																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>27,314</u>																													
<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 5</td><td>FE</td><td>2793</td></tr> <tr><td></td><td>ME</td><td>15,801</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>28,254</u></td></tr> </table>	YEAR 5	FE	2793		ME	15,801		TW	4000		PCF	5660		<u>TOTAL</u>	<u>28,254</u>	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 6</td><td>FE</td><td>2996</td></tr> <tr><td></td><td>Me</td><td>16,592</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>29,248</u></td></tr> </table>	YEAR 6	FE	2996		Me	16,592		TW	4000		PCF	5660		<u>TOTAL</u>	<u>29,248</u>
YEAR 5	FE	2793																													
	ME	15,801																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>28,254</u>																													
YEAR 6	FE	2996																													
	Me	16,592																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>29,248</u>																													
<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 7</td><td>FE</td><td>3211</td></tr> <tr><td></td><td>ME</td><td>17,421</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>30,292</u></td></tr> </table>	YEAR 7	FE	3211		ME	17,421		TW	4000		PCF	5660		<u>TOTAL</u>	<u>30,292</u>	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 8</td><td>FE</td><td>3444</td></tr> <tr><td></td><td>ME</td><td>18,292</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>31,396</u></td></tr> </table>	YEAR 8	FE	3444		ME	18,292		TW	4000		PCF	5660		<u>TOTAL</u>	<u>31,396</u>
YEAR 7	FE	3211																													
	ME	17,421																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>30,292</u>																													
YEAR 8	FE	3444																													
	ME	18,292																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>31,396</u>																													
<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 9</td><td>FE</td><td>3693</td></tr> <tr><td></td><td>ME</td><td>19,207</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>32,560</u></td></tr> </table>	YEAR 9	FE	3693		ME	19,207		TW	4000		PCF	5660		<u>TOTAL</u>	<u>32,560</u>	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>YEAR 10</td><td>FE</td><td>3960</td></tr> <tr><td></td><td>ME</td><td>20,167</td></tr> <tr><td></td><td>TW</td><td>4000</td></tr> <tr><td></td><td>PCF</td><td>5660</td></tr> <tr><td></td><td><u>TOTAL</u></td><td><u>33,787</u></td></tr> </table>	YEAR 10	FE	3960		ME	20,167		TW	4000		PCF	5660		<u>TOTAL</u>	<u>33,787</u>
YEAR 9	FE	3693																													
	ME	19,207																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>32,560</u>																													
YEAR 10	FE	3960																													
	ME	20,167																													
	TW	4000																													
	PCF	5660																													
	<u>TOTAL</u>	<u>33,787</u>																													

Grand total = \$289,621

Total Profit 10 yrs. = \$214,621 (\$289,621- \$75,000 =\$214,621)

Monthly Profit = \$1788.51

(214,621 divided by 120)

NET MONTHLY INCOME = **\$1788.51**

Rate of return for Rental Property Investment

Calculated as (value now - value at time of purchase) / (value at time of purchase)

Rental property

Value Now- \$ 289,621

Value at time of purchase- 75,000

\$289,621 -75,000= \$214,621

214,621 divided by 75,000= **10 Year Return 286 %**

As the figures clearly show if I took my \$75,000 and invested it in a rental property for 10 years I would have \$289,621 a gain of \$214,621 or an average monthly gain of \$1788.51. In 10years I have increased the value of my money by 286 %. And 20 years from now (or sooner if I discipline myself and make regular unscheduled principal payments) when this asset is paid off , I will get a bonus for my patience, I will gain an additional \$1384 per month (when the mortgage is wiped out). This bonus will arrive just in time to make me retire like a well compensated King.

The numbers don't lie, the jury's verdict is in- the rental property investment is the clear winner.

Rate of Return

- Regular savings account- 10 year return 22 %
- Certificates of deposit/Government bonds- 10 year return 96.7 %
- Index fund (Mutual fund/Stocks) 10 year return 211%
- Rental property 10 year return **286%**

I now feel comfortable investing in a vehicle that made my old man obscenely wealthy because I took the time out of my valuable existence to confirm the validity of this highly touted wealth building product. The hesitation of being an aggravated landlord has been eradicated by the indisputable proof of it's superior investment potential. I have proved to myself that the aggravation of being a landlord pays big dividends. I have not disproved the merits of other investment vehicles. They are worthwhile financial products and should be used in conjunction with the rental property investment. A true King of the middle class is a well diversified investor, whose financial basket includes many wealth building products. My aim is NOT to have you invest solely in rental properties; but to add it as one of the many eggs in your investing basket. I purposely made sure I didn't exaggerate or fluff the numbers or bend my research to accommodate this endeavor. I wanted to paint an accurate picture of the rental property investment. I wanted to show how real estate performs in bad times not good times. I purposely omitted the high appreciation rates that ripped through this country the past 7-8 years. In New York we experienced almost quadruple the

appreciation rate that I used to judge the rental property. I purposely did this to quiet any skeptics who might infer that real estate as an investment only generates a high return in a highly appreciating seller's market. I wanted to show the darker side of real estate, how it performs in a buyer's market, devoid of double digit appreciation jumps. I did this because the buyer's market is coming and I want you to be prepared to prosper by providing you with the right information; so you can logically invest in this vehicle without relying on inflated or unrealistic expectations. My old man taught me well ,he said, "the trick to investing in real estate is to invest in the bad times so you can reap your just rewards in the good times ". You want to be buying when people are selling, and selling when people are buying.

You want further proof of the power of real estate as a viable investment, don't take my word for it or my old man's word for it, just ask another obscenely wealthy investor, Long Island's own , Charles Wang. Charles Wang had access to all the resources of the investing world, a direct plug into wall street, and when his company Computer Associates went public and he made a gazillion dollars, aside from his other investments he bought half of Glen Cove , a prestigious town in Long Island. Obviously Charles Wang knew what the old man knew- real estate is a powerful wealth building vehicle that can drive you to a personal fortune.

Now that I was sold on the merits of real estate as a sound financial investment, I reflected back on the notes I took with the old man while he was alive in Southside and began to piece together his system of how to invest in real estate. I knew most of it from investing with him, but I transcribed his thoughts to paper as good measure lest I forget any crucial details. The old man said the best way to invest in anything is to do your research first and then develop a sound plan of action. The research part gives you the confidence you need to successfully carry out the plan without the hesitation of self doubt. You will never invest your hard earned dollars in something unless you are 100 % confident that it is the right thing to do and that it will make you more money. The old man said he learned this valuable lesson his first year in real estate, from his mentor Raymond J Connor of the Housing Exchange in Brentwood NY. The old man said Ray, his sponsoring real estate broker, approached him with an opportunity to invest in something quite foreign to him at the time, an FHA cashover. Ray wanted the old man to fork over \$2500 cash and partner up on a house with him. The old man said he balked because his ignorance of the profit potential of the FHA cashover stopped him from participating in the venture. This turned out to be a \$7500 education for the old man , when weeks later Ray resold the same house for a tidy \$15,000 profit. The old man apologized to his mentor for not believing in his judgment. His mentor turned to him and said, "Harry , real estate is a self taught business, you will only make the big bucks in real estate when you feed your mind with books, tapes and seminars that give you the education and comfort level you need to successfully invest your money." The old man said , "from that day forth, I had 7500 reasons to fill my empty head with as much real estate knowledge as I could get my hands on." The old man said , the system I am about to unfold to you son is the culmination of those years of learning and earning I did with the greatest teacher of all, myself. The old man said, I pay respectful homage to my mentor Raymond J Connor who was adroit enough to make me realize that. My old man said that Ray told him "one day in the future harry, you won't thank me for your riches, that distinct honor will be bestowed on you and the knowledge you filled your head with that got you there." The old man said, I give that same advice to you son, don't feel compelled to thank me for your wealth that honor falls on you for being stupid enough to listen to your old man and profit from his wisdom.

The Plan

- Buy Appreciating Assets. (Something that you buy today that in all likelihood over time will go up in value and cost you more to buy the same thing tomorrow) ie Real Estate A Car is just the opposite- a depreciating asset. The time frame is the trick. In real estate the time frame changes depending on when you initially invest. In a highly appreciating market (a sellers market) 1-5 year hold is all it takes. In a slowly appreciating market (buyers market) it may take 10 years or more to see the same profit potential.

Real Estate

- Hold it for a minimum of 10 years
- Tenant pays all Bills
- You get all Tax Write-Offs
- You sell for Profit or Refinance (tax free) or you hold it for the rest of your life- and retire like a king by collecting Positive Cash Flow Income from your **Pension Walker's** or exchange (1031 tax deferred exchange) for even greater positive cash flow.

END GOAL- Have 2-4 properties paid in full and enjoy 4000-6000 per month in **Passive Income**.

After doing what my old man instructed me to do (researching) I have added a thing or two to the Plan.

- Invest in the stock market or mutual funds via **Index Fund**. How could I ignore the logic of an investment that I proved to myself can increase the value of my money by 211 % in 10 years. It came in a respectable 2nd place to my core investment vehicle, real estate rentals and it definitely warrants the allocation of my investment dollars.
- Invest in tax free municipal bonds to offset the future expenditures of your children:
 1. Sweet 16 Parties
 2. High School graduation parties
 3. New Cars/car insurance premiums for your kids
 4. College educations
 5. College graduation parties
 6. Weddings
 7. Grad school education
 8. Down payments for their first home

You should structure these investments based on the ages of your children
So when the money needed has to be allocated, its there.

The old man said every Plan has to have it's rules. These are the rules I established as a real estate investor from years of trial and error. I only added to his rules any applicable post 1997 (the year of his death) stratagems.

The Rules

- Rental Property(Bare minimum)
3-4 Bedroom ranch with full basement
- Always try to maintain a 10,000 – CASH RESERVE FUND PER HOUSE – so you can sleep at night. Whenever you tap it try to replenish it.
- Time Horizon- 10-15 years.
Allows a professional investor to realistically experience and profit from both a seller's market and a buyer's market. The professional knows : Instant riches (“get rich quick”) are the result of years of focused dreams. The real millionaires reach their destination usually after 10-15 years of smart investing.
- Below average/ low property taxes on rental.
- Positive Cash Flow- (Bare minimum)- 200 per month- NO EXCEPTIONS- (protects you from down market, when rents could go down)
- Always try to increase your positive cash flow
- Always be a disciplined saver and make unscheduled principal payments. The sooner you get your **Pension Walker**, the sooner you can realize your dream of retiring like a King at an early age.
- Always pre pay interest only non amortized loans.
- Always refinance your way to increased positive cash flow
- Always sell or trade your way to increased positive cash flow
- Always protest your property taxes for increased positive cash flow
- Always take full advantage of any and all property tax exemptions available in your locality. They will **respect** you for your knowledge and oft times **reward** you with lower property taxes.
- **Minimum Paid off Positive cash flow**- 1000 per month per rental- when house is paid in full you must make bare minimum 1000 in pocket after paying prop tax and ins. Or don't buy . Otherwise You won't respect your pension walker .
- Always use a **Line of Credit** on your primary residence as your personal piggy bank for short term flips. Also it is good cover for the King of the middle class lifestyle.
- Only use **interest only** loans in isolated circumstances and stay away from the dangers of **ARM's**.
- Always pay your bills on time : a good credit rating is the fuel that powers your financial vehicle.
- **Incorporate** your holdings to add professional distance, a liability shield and increased tax write-offs.
- Never invest in **rent control/rent stabilization** areas- it is an eviction nightmare
- **Evictions**- Always hire a lawyer to go to court for you and never fight for the money always fight for possession.
- Always **invest in tomorrow not just today**.

The Old man used to say, People who buy homes to live in, and raise families in are investing in **today**. These are not investors these are homeowners. They need a place to live today.

People who invest in houses and rent them out to other families to live in are investing in tomorrow. These are investors that are holding assets that hopefully will appreciate in value and pay them **tomorrow**.

That's why you don't break up houses like the slumlord, who invests only in today's profits. You are a professional landlord, you play by the rules and profit from tomorrow's higher returns. You don't get involved in illegal basement apartments, these are for the amateur landlords or strapped homeowners who blindly invest for today's profits. These amateurs are one complaint away from a possible \$5-10,000 legal problem that you as a professional will never have the honor of experiencing. Legal rents that guarantee a steady flow of passive income for a kingly retirement is the reward the professional landlord, like you, gets for investing in tomorrow.

- **Location/Location/Location**

Always remember whatever you buy you eventually must sell so if you get a bargain price on a property in a poor location in a hot sellers market (busy street great neighborhood) you may have a problem liquidating this Undesirable property in the cold buyers market that is coming. (Psst if the bargain price is greater enough to justify the risk I am in)

- **Always consult your Detractor Checklist when investing in a rental (take value away)**

Burn out

Board up

Wreck

Busy Road

Lot Size

Excessive Repairs

Neighborhood

Near Commercial

Small House (less than 3 BR)

Small House (less than 900 sq ft)

No Basement

No Garage

Corner Lot

Back Yard Size

No Rental unit

Low wires

Flood Zone

Rodents(deer,rats,mice, etc...)

- **Repairs-** In a sellers Market buyers fight over Handiman Specials- the concept of fixing up property and activating the inherited equity. In a buyers market the real bargains exist in houses already fixed to the nines – saving you the time and expense of repairs . These same houses would command a premium in a sellers market.(Exception to rule Handiman house so severely discounted you cant say No)

It is better not to buy rentals in a buyers market that need heavy repairs you never know how long it will take to recoup the money. You want to fix your properties in a sellers market , where cost of renovations are justified by increasing values. Translation : A professional real estate investor buys beat up rentals at a bargain price in a buyers market and sticks around long enough to fix up and unload investment in new seller's market. The professional investor accomplishes this by investing with a realistic timeline of 3-10 years, so time can make the above event a realized dream.

- **Home Inspection (monster negotiating tool)**

In a red hot sellers market this negotiating tool was all but wiped out. If you found serious defects in a house you were buying the agent would just sell house to less discriminating buyers waiting in the wings to outbid you on this gem. In a buyers market the seller will either adjust price against defects or risk losing the sale. The inspection will also be a guide to estimating fix up costs on rental.

Roof
Exterior (vinyl siding)
Windows
Doors
Kitchen
Bath
Plumbing
Electrical- outlets/switches/fixtures
Service (100amp/200amp)
Floors
Boiler
Cesspool
Molding
Landscaping
Appliances
Spackling
Painting
Extermination

Invest Local – 30-40 minute drive max. – this was my old man’s comfort zone. He said, ” once you stray out of this zone you are more likely to bail on your investment before it bears it’s ripest fruit. The old man said, I made that mistake in Florida- it’ll never happen again.

- **PREPARE YOURSELF FOR THE APPRECIATION DOWNTIME**
And Don’t Panic.(The Greenspan Effect)

438,950 value @ 6% (5 %down) payment– 417,000 mortgage 2502
300,000 value @ 10 % (5 % down) payment –285,000 mortgage
2502

Affordability is the issue. Same house has 2 different values depending on interest rate.(roughly same payment 2502) If you bought house at top of the market (438,950) and followed the rules of 200 min Pcf - you still win; the PCF and tax write offs and forced equity will eventually make you a winner. If rates go up DON’T PANIC you will lose equity; theoretically you could lose up to 140,000 based on affordability. But the smart investor knows that the same house could easily go back up to 440k when the rates go down again.(and then some)What comes down must come up and vice versa.

- **Follow the FHA loan limits when investing**
AFFORDABLE MARKET VALUES

- **Your Maximum Buy Price Has been set for 1-4 family houses**

The Federal Government does not actually lend out the money, licensed mortgage bankers and banks lend out the money based on underwriting criteria set by the FHA. The FHA insures the repayment of the money by charging each borrower a MIP (mortgage insurance premium). The FHA decides how

Tim Larkin
King of the Middle Cass
www.rkrnys.com

much money to allow lenders to lend in each area by putting caps on loan amounts in each area in each state.

The FHA mission is to make homeownership an affordable and possible dream for every qualified American. The FHA has low down payments (2.25%) and allows imperfect but explainable credit blemishes.

If you default on a FHA loan the lenders, as directed by the FHA guidelines, have to bend over backwards to help you. The loan repayment is fully insured so the lenders are really not in jeopardy of losing any real money. The lenders will not receive a dollar of that money unless they abide by the rules of default set by the FHA. The rules change from time to time but they usually involve mandatory counseling and restructuring of payments (adding arrear payments to principal balance and recalculating new P&I)

Translation: the government provides affordable housing by insuring lenders who lend money to otherwise risky borrowers. The FHA borrower puts little down (as little as 2.25%). (The government is even toying with the idea of 0% down) The buyer usually has bad, but explainable credit; usually has a much lower FICO Score; and is afforded probably the highest form of protection in a foreclosure action.

*After the events of 9-11 the government imposed Mortgagee Letter 2001-21 giving “affected borrowers” a 90-day moratorium on any foreclosure action on their FHA Mortgage.

The government with all its intelligence and resources has decided to do all the homework for the average investor. The government has decided in numerical form what affordable is in each area of our wonderful country. An astute investor only wants to buy what is affordable. Now the investor has a benchmark a reference point to determine affordability. (**see chart**). A good investor knows what is affordable today could be out-priced tomorrow. These government limits are not the *Fair market values* in the areas; they are the *affordable* market values in the area. The price of the property in a given area that the government feels confident enough to insure against loss from default.

This Free info from the government provides a **fixed price** that an investor can establish as the affordability ceiling in the area in which she plans on investing.

For example- Suffolk – 312,895

If you find a house at or below this mark it may if it meets all the other **rules** we have established be a good candidate for a rental property investment.

If the house is above this price DONT BUY IT- unless somehow it can meet our RULES OF INVESTING.

FHA home mortgage loan limits - New York

County	MSA	1 Unit Loan Limit
ALBANY	ALBANY-SCHENECTADY-TROY, NY (MSA)	\$172,632
ALLEGANY	NON-METRO	\$172,632
BRONX	NEW YORK-WAYNE-WHITE PLAINS, NY-NJ METROPOLITAN DI	\$312,895
BROOME	BINGHAMTON, NY (MSA)	\$172,632
CATTARAUGUS	OLEAN, NY (MICRO)	\$172,632
CAYUGA	AUBURN, NY (MICRO)	\$172,632
CHAUTAUQUA	JAMESTOWN-DUNKIRK-FREDONIA, NY (MICRO)	\$172,632
CHEMUNG	ELMIRA, NY (MSA)	\$172,632
CHENANGO	NON-METRO	\$172,632
CLINTON	PLATTSBURGH, NY (MICRO)	\$172,632
COLUMBIA	HUDSON, NY (MICRO)	\$172,632
CORTLAND	CORTLAND, NY (MICRO)	\$172,632
DELAWARE	NON-METRO	\$172,632
DUTCHESS	POUGHKEEPSIE-NEWBURGH-MIDDLETOWN, NY (MSA)	\$270,750
ERIE	BUFFALO-NIAGARA FALLS, NY (MSA)	\$180,500
ESSEX	NON-METRO	\$172,632
FRANKLIN	MALONE, NY (MICRO)	\$172,632
FULTON	GLOVERSVILLE, NY (MICRO)	\$172,632
GENESEE	BATAVIA, NY (MICRO)	\$172,632
GREENE	NON-METRO	\$172,632
HAMILTON	NON-METRO	\$172,632
HERKIMER	UTICA-ROME, NY (MSA)	\$172,632
JEFFERSON	WATERTOWN-FORT DRUM, NY (MICRO)	\$172,632
KINGS	NEW YORK-WAYNE-WHITE PLAINS, NY-NJ	\$312,895

Tim Larkin
King of the Middle Cass
www.rkny.com

	METROPOLITAN DI	
LEWIS	NON-METRO	\$172,632
LIVINGSTON	ROCHESTER, NY (MSA)	\$185,250
MADISON	SYRACUSE, NY (MSA)	\$172,632
MONROE	ROCHESTER, NY (MSA)	\$185,250
MONTGOMERY	AMSTERDAM, NY (MICRO)	\$172,632
NASSAU	NASSAU-SUFFOLK, NY METROPOLITAN DIVISION	\$312,895
NEW YORK	NEW YORK-WAYNE-WHITE PLAINS, NY-NJ METROPOLITAN DI	\$312,895
NIAGARA	BUFFALO-NIAGARA FALLS, NY (MSA)	\$180,500
ONEIDA	UTICA-ROME, NY (MSA)	\$172,632
ONONDAGA	SYRACUSE, NY (MSA)	\$172,632
ONTARIO	ROCHESTER, NY (MSA)	\$185,250
ORANGE	POUGHKEEPSIE- NEWBURGH-MIDDLETOWN, NY (MSA)	\$270,750
ORLEANS	ROCHESTER, NY (MSA)	\$185,250
OSWEGO	SYRACUSE, NY (MSA)	\$172,632
OTSEGO	ONEONTA, NY (MICRO)	\$172,632
PUTNAM	NEW YORK-WAYNE-WHITE PLAINS, NY-NJ METROPOLITAN DI	\$312,895
QUEENS	NEW YORK-WAYNE-WHITE PLAINS, NY-NJ METROPOLITAN DI	\$312,895
RENSSELAER	ALBANY-SCHENECTADY- TROY, NY (MSA)	\$172,632
RICHMOND	NEW YORK-WAYNE-WHITE PLAINS, NY-NJ METROPOLITAN DI	\$312,895
ROCKLAND	NEW YORK-WAYNE-WHITE PLAINS, NY-NJ METROPOLITAN DI	\$312,895
SARATOGA	ALBANY-SCHENECTADY- TROY, NY (MSA)	\$172,632
SCHENECTADY	ALBANY-SCHENECTADY- TROY, NY (MSA)	\$172,632

Tim Larkin
King of the Middle Cass
www.rkny.com

SCHOHARIE	ALBANY-SCHENECTADY-TROY, NY (MSA)	\$172,632
SCHUYLER	NON-METRO	\$172,632
SENECA	SENECA FALLS, NY (MICRO)	\$172,632
ST. LAWRENCE	OGDENSBURG-MASSENA, NY (MICRO)	\$172,632
STEUBEN	CORNING, NY (MICRO)	\$172,632
SUFFOLK	NASSAU-SUFFOLK, NY METROPOLITAN DIVISION	\$312,895
SULLIVAN	NON-METRO	\$172,632
TIOGA	BINGHAMTON, NY (MSA)	\$172,632
TOMPKINS	ITHACA, NY (MSA)	\$172,632
ULSTER	KINGSTON, NY (MSA)	\$223,250
WARREN	GLENS FALLS, NY (MSA)	\$172,632
WASHINGTON	GLENS FALLS, NY (MSA)	\$172,632
WAYNE	ROCHESTER, NY (MSA)	\$185,250
WESTCHESTER	NEW YORK-WAYNE-WHITE PLAINS, NY-NJ METROPOLITAN DI	\$312,895
WYOMING	NON-METRO	\$172,632
YATES	NON-METRO	\$172,632

http://www.fhalibrary.com/fha_mortgages/fha_loan_limits/new_york.asp

- Always remember the market you are investing in. If you are investing in a **Seller's market** use **Yesterday's Game**, if you are investing in a **Buyer's market** use **Today's Game**.

<u>Yesterday's Game</u>	<u>Today's Game</u>
Appreciation/Mtg. Leverage	Instant Equity/Free & Clear
NO \$ DOWN	20% DOWN/ Short Sale
LEVERAGE: <i>Investing with borrowed money as a way to amplify potential gains (at the risk of greater losses)./ARM / INT ONLY(No Equity)</i>	Instant equity: (DP is equity)
Rent	Rent
Hold (1-5years)	Hold (5-10 years)
Short-term Buy as many houses as Possible with as little as possible Down (LEVERAGE) and ride the Appreciation Wave Or Flip and cash out.	Short-term Buy 2 rental properties with healthy PCF , wait for market to appreciate, sell one pay off /down Mtg. On other one OR FLIP properties using SHORT SALE. *
Long-term Own many rental properties with Little or no Positive cash Flow and Wait for Market to Appreciate and Cash Out.	Long-term Own 1-2 rentals, paid-in-full; and then Retire Early; and ride the PCF Wave.
NEGATIVE CASH FLOW Investors	Positive Cash Flow Investors Min 200 PCF- Flexible sellers- HOLD PAPER / PAY CLOSING COSTS
Lose 500-1000 month/ property appreciates At 30-40k year – cash out #1 REASON INVESTORS LOSE \$\$ IN REAL ESTATE- APPRECIATION GREED (article – conservative investor- Jim Gillespie PH. D.	Welcome to the Buyers Market <ul style="list-style-type: none"> • Real Sellers Concession • Seller Held Financing • Negotiable sellers • Home Inspections that matter • Short Sale Bonanza

* A Short sale is when a lender avoids the prohibitive costs of a foreclosure by cutting their loss and accepting less than what is owed to them in order to satisfy the lien on the property.

Most common conditions for a successful Short sale :

1. Borrower in foreclosure
2. Neglected property- in need of repairs
3. Slow moving Buyer's market

***How to do a Short Sale**

- Contract of sale- non-involved party.
- Contact loss mitigation dept. of lender.
- Title report- Check for : Back taxes, judgments, other mortgages, ownership info on deed.
- Hardship letter- detailed account of reasons for default .
- Broker Price Opinion- establishes lender value.
- Estimation of repairs- provide photos to substantiate.
- HUD 1- Fill out estimated HUD 1 detailing anticipated closing costs. Must show \$0 going to borrower. The estimated HUD 1 justifies maximum payoff amount to lender. (the HUD 1 in a short sale always allows a little wiggle room for a real estate broker to charge a commission for providing this valuable service)

- **Minimal Education Requirements**

Rental Values- necessary to establish realistic PCF

Resale Values- necessary to establish buying & selling Price

Fix-up costs- necessary to establish bottom line buy Price

You must know the market you are investing in. You must know what the houses are worth in your investment area, what the typical rents are and how much it realistically costs to rehab your investments.

How to play Today's Game

- **Run Credit-** establish fico score and borrowing power.
30 year Mortgage- Fixed not adjustable. 1-year pre-pay penalty
- **20% Down Payment(Asset Check)**
Primary Sources:
 1. Cash
 2. Line of Credit – Sister company Sonline Funding Corp.- take equity out of primary residence use to invest.(used primarily for flips but can be used for rentals if PCF requirements are met) Translation: If you can still make a \$200 PCF factoring in the added indebtedness of a line of credit payment; buy and prosper.
 3. Borrow from people who know you and trust you.(0% interest)
 4. Borrow IRA(talk to your CPA)
 5. Sell underperforming stocks, bonds, mutual funds etc.
 6. Relationship Selling- use \$ to buy rentals.
- **Follow the RULES(criteria for rental)**
- **Hunting for rental-**MLS, FSBO, estates, Handiman specials, Lis Pendens
- **Acquisition of rental-** contracts, mortgage, insurance, estimated fix up, legal & accounting ramifications
- **Renting rental-** advertisements, qualifying the tenant, preparing lease

**Shopping for a Property Manager?
Look No Further!**

TRUST



**Call RKR TODAY!
631.440.6969**