SCENARIO – A PACTRUST™ DEAL FROM BEGINNING TO END.

By Bill J. Gatten

I received a call from my partner's bandit sign ("I Buy Houses, Full Price, All Cash or Terms Any Condition, Any Price")

The caller is a Mr. Sam Brown who says he has a house in Mission Hills, Ca. that is worth maybe $150,000, but which has a $154,000 loan on it and work to be done. I ask him "what he would like to see happen." He says he is just looking for someone who would take over his payments. I then ask how much work needed to be done. He says maybe $10,000 worth. My comment is: "Phew Doggies!"

Next, I ask how far in arrears his payments are. He indicates that they are current…for the moment. I then ask what he would do if I were not able to help him. His comment is that he just wants to walk away, and that he has no cash and will not be making any further payments, irrespective of whether I take the house or not.

I tell him I'll call him back the next day after checking the title and getting some comparable value information together (comps). The comparable sales in the area show the property to be worth perhaps $155K to 160K after fix-up (still no equity for me).

March 15:

I call Mr. Brown and arrange to meet him at the property that same day.

After seeing the mess (broken windows, a yard full of trash, weeds up to the windows, windows frames that didn't meet the walls, peeling linoleum on the floors, dry-rot and termites), I comment to Mr. Brown that I can see that he is truly in a pickle on this one...he agrees and reiterates (in case I didn't hear him the first time) that he has no money and has no choice but to let it go back to the bank if I don't want it.

After inspecting the house, I determine that actual costs to bring the property to a reasonable cosmetic condition (with good, but cheap, labor and parts) might run no more than $6,000 to $7,000. I reason, as well, that by keeping the loan in place and asking for $10,000 up front from a resident co-beneficiary on a 50:50 equity share, I can get all the work done and perhaps have a little left over. I figure I can advertise it at $165,000 and perhaps be able to start out at break-even (without cash out of pocket) and with a couple thousand in my wallet.

I then have Mr. Brown sign a 15-Day Option to give me 15 days before I have to make my final commitment (I try for 30, but he's afraid of having to make another payment…I know, bad logic…he was never going to make a payment anyway). Upon handing him the Option to sign (with a dollar bill stapled to the front), I also give him an unsigned copy of the Purchase Offer (Appendix #1 of the 10-Step Process of Documentation

Manual), explaining that the dollar is just legal consideration (‘stops them from asking for an option fee).

March 16:

I beat it to the county court house and recorded the Memorandum of Option, then over to the newspaper office to run my ad:

NO BANK QUAL
NO DOWN
NO CRED. APP
3 Pmts and Clos Costs
Moves you in. Nice $165K 3+2
Home. Needs TLC. xxx xxx xxxx

March 18:

I have my friend “Bob” put a coat of gray paint on the front of the house and have him frame all the window and door openings with 1 X 6 boards. He then paints all the trim a nice bright white. We then take all the trash that is in the front yard…and throw it all in the back yard. Next, we Roto-Till the front yard and plant some flowering bushes along the front of the house and along the walk. After two or three hundred dollars at most, the house looks quite “cute and cozy (as they say)” FROM THE STREET (‘called “Curb Appeal”). The plan is to THEN (and only then) begin work on the rest of the house, in hopes that someone might just drop by and offer to do the rest of the work for a reduction in price, before I’ve had to spend much more money.

March 20:

Bob dismantles the “things” that will eventually have to be repaired (e.g., ‘pulls the tub away from the wall where the dry rot is, removes the window sills that don’t meet the wall, takes the doors off the kitchen cabinets that are to be resurfaced, etc. (no work, just partial dismantling…creating the illusion of “work in process,” so to speak). Note that even though I haven’t exercised the Option, I’ve spent about $400 at this point for everything.

March 24:

After the front of the house is cleaned up, and once the ad hits, the phone calls start hitting my answering machine, one after another. I call them all back and repeat the same mantra over and over again with every caller:

“Yes, I have this great little house over there on Xxxx Street in Mission Hills, and if you can afford the nine or ten thousand that it’ll take to get in, and the $1,200 or so in monthly payments…after you add the tax and insurance, of course: I’ll just GIVE it to you (pause). The only thing I want out of it is to have you put it in your own name, or sell it, in a few years, and at that time if there's been any appreciation I'll just split it with you." (NOTE: If they don't like the 'split appreciation' idea, you can say, "No problem. If you'd prefer, you can come in with $18,000 instead of $9,000 and you can have it all." They invariably want to get back the $9,000 deal.)

With each caller, I tell them that the house is being worked-on at the moment, but that if they want to see it, they have to come "with their rose colored glasses on," because it's a real mess at present." I tell them that we haven't had a chance to do much of anything yet…or even haul off the trash. Then when they show up, I make sure that my buddy Bob has tarpaulins and plastic sheets spread out over the floors and counter tops, and that paint cans can be seen in various places (needs to look like something's going on). With all of the callers, I tell them to drive by the house and then call me if they like it from the street and have an interest (Remember…the place looks great from the curb: I want them to see it from the street, then begin rationalizing all the shortcomings and building their "want-to" while they sleep that night).

March 26: The fifth or sixth caller calls back and asks if we can meet at the house to work something out. Maybe 7 or 8 others have said they'll drive by, but haven't yet. I know we've got a live one at this point. I again remind the prospect that the house is a mess and that he'd better have a good imagination for "potential" and for what things COULD be like, rather than what they ARE like. He laughs and agrees and we meet.

After an inspection of the mess, he asks when I might be finished with all the work…I tell him maybe as much as two months (I know he'd like to move as soon as possible). He seems discouraged. I then tell him that if he'd like to finish the work himself, I'll knock a couple thousand off the price and, say, $2,500 off the amount I need from him to get into the property (i.e., now he can get in for $5,000 plus the first payment when it comes due).

I fill out a purchase offer--from him to me--and have him sign it and accompany it with certified (non-refundable) funds in the amount of at least one full monthly payment obligation $1,200 ('could be any amount you specify).

March 27:

I return to Mr. Brown, the seller, in order to give him my signed (and already accepted) purchase offer. First, however, before giving him the paperwork, I tell him that the property is a lot worse than I had first thought. I see him wince a little. At that point I tell him about the termite problem and tell him that he'll need to pay the $2,000 for the tenting and spraying, but that I'll take care of everything else. He heaves a sigh of relief and agrees, assuming that I'm paying the $10,000 that he estimated to cost to be and that I'm also paying all costs of marketing ('when they say they don't have money, what they mean is: I have some, but I don't want to spend it unless you pull the right levers).

April 1:

The property is tented…at Mr. Brown's expense. The poison is sprayed, the termites begin singing "Cum Bah Ya" as they weaken and are no longer able to hold hands; and as their grip fails them and their little arms fall to their sides, the house crumbles and falls down (no, just kidding…they all die and go to termite Heaven, I'm sure).

April 10th.

I complete the paper work for the "Joe Brown Land Trust" and have Mr. Brown execute the document (as the only beneficiary), thereby appointing PAC Holdings as the trustee.

April 11th:

I complete the "Assignment of Beneficiary Interest" agreement from Mr. Brown to my resident co-beneficiary and me. I then complete the "Beneficiary Agreement" between us. The Beneficiary Agreement designates our percentages of ownership of the beneficiary interest in the trust as: 10% to Mr. Brown; 40% to me; and 50% to the Resident Beneficiary. However, I arrange to have it stipulated in our agreement that Mr. Brown will forfeit his 10%, and any claim to profit, to me at termination (I just need him to hold onto it for now in order to avoid Due-on-Sale Clause issues, reassessment of property tax and the payment of transfer tax upon. Note here as well, that I leave Mr. Brown with 50% of the voting rights so as not to invoke property tax increases, reassessment and conveyance tax: but I take a Power of Attorney from him so that I can vote his rights and not have to involve him in management decisions.

May 1st:

The resident co-beneficiary brings the rest of his money to Escrow, signs all documents, makes his first payment on the contract and is given the keys to the property.

May 2nd:

The deed to the trustee is recorded; a triple-net lease agreement between the Trustee (PAC) and the resident beneficiary is executed and the resident-beneficiary moves into the property and/or starts his work on the property (i.e., "takes possession").

All signed documents are sent to the trustee, who retains the collection service who sets up the transaction and begins payment collections and disbursements for the term of the agreement.

May 4th:

I receive a check in the mail for $5,000, less the cost of Escrow, title search, IRS filing fee, and a one month Contingency Fund (to be used to kick the co-beneficiary out if I ever have to)

Now, when the trust and the accompanying lease agreement terminates, the property will be sold; all costs of sale will be paid; I will get back the equity that I carried (the difference between the loan amount at start and the $160K the resident came in at; the resident beneficiary will receive a refund of his $5,000; and all remaining proceeds will be divided between the resident beneficiary and me.

August 22, 2001:

So far (2 years into the deal), that property has increased in value to about $210,000; I receive a $100 positive cash flow each month; the loan has paid down by about $3,600. I therefore have earned approximately $33,000 on an over-encumbered property that no one else wanted, and which involved No Down Payment, No Credit Application; No New Loan; No monthly payments; No management; No maintenance, No up keep or refurbishment costs. Furthermore, the lender's Due-on-Sale clause was not violated; the property is protected from credit and tax liens, bankruptcies of any party; marital dispute actions of any party's spouse and Probate should any party die.

Cool, eh?

Bill Gatten