What to do with my money

Everything you wanted to know about Real Estate But didn't know what to ask

WHAT IS REAL ESTATE?

When we use the term real estate, we are talking about buying a piece of physical property, a building, piece of land, or even a part of a building (like a condo). It can include buying and owning vacant land, a home, commercial building, condominium, or even a part of a dock you can own to park your boat. There are three terms generally used.

1. Fee Simple. This means that if you buy it, you own the property and anything on the property until you, or your ancestors sell it. The only exception is in some states you do not own the right to any valuable minerals, say gold or oil, that are found on the property.

2. Lease Hold. This is where some corporation, individual or government owns the land, but you buy a "long term lease" and can use the land and buildings anyway you see fit. This can save you money from putting up large buildings, and allows you to move into industrial and "great location"areas, which are typically only available on leased land (very common in Hawaii, and ocean front properties). Sometimes properties are sold with just a few years left on the lease, and it's up to you to renegotiate with the owner when the lease is up. The good thing about a long-term lease is there are some positive tax implications for companies, are cheaper in the long term than renting, and the owner of the lease usually gets to be the first person to renegotiate the lease when it expires.

3. Lease with an option to buy. This is the same as leasehold, but at a certain point you are able to buy the property outright. This is more common in residential homes, since the owner can get a larger deposit, which secures the lease, and then regular rent money each month. The buyer benefits because they get the chance to buy a home without having a large down payment required by most banks. They can also break the lease if they decide they don't want the home, but forfeit their initial large deposit.

WHAT KINDS OF REAL ESTATE SHOULD I LOOK AT?

When you purchase, or sell a property, the government basically dictates what can be done on that property through zoning laws. Some property zoning requirements can be changed, which we will cover later. Some areas are also called mixed-use where a mixture of properties can be found in a small area. When it comes to what kind of real estate you should buy, it is important to determine why you are buying it.

1 The first questions you should ask are: "Do I want to live there with myself or my family, use it for income, start a business, work with large groups of animals or plants, or even start some large business endeavor. Remember each one of these questions will determine what type of property you need.

2 The next question is how much can you afford. Most people do not buy a property outright, but negotiate some type of payment system with a bank, institute, or even the property owner. Remember you need to have enough for the down payment (10 – 30%), and good enough credit to get a loan (determined by a number system called a credit score). Without these it'sawfully hard to buy a property.

When it comes to real estate there is basically three categories (called zones):

1. Residential: This includes any type of land or building that is primarily used as a living space. Basically they include land or buildings designed for single family and multi-family living spaces.

2. Commercial/Industrial: This includes land or buildings that can be used to sell, manufacture, or develop anything that is bought and sold. Commercial land and buildings can be grouped in a specific region, or scattered around residential areas and include stores, malls, shopping centers, offices, and wholesale/retail outlets. Industrial land and buildings are mostly found in a certain areas where larger manufacturing, processing, product development, and mining facilities are found.

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3. Agricultural: These include typically rural areas where you find farms, ranches, vineyards, orchards and other areas that have plants and animals used for consumption. When you buy an agricultural property it's important to find out what you can build on the property, since most agricultural property must have residential/commercial clauses written into the zoning requirements for the building of a home to live in, or a place to sell your items.

DOES IT MATTER WHERE I BUY, AND IS IT BASICALLY THE SAME IN EACH COUNTRY?

Everything bought or sold in the world is done on some type of market. The Real Estate Market is no different, and there are many people out there to help. It also depends on real estate laws practiced in each country. It would take a long time to discuss the rules in each country, and sometimes they change radically country to country. There are a few things to remember.

1. How stable is the country or area in which you are buying. Unstable countries can change entire governmental structures, and you could lose the property, or even be held accountable for what is done on the property even if it was legal before. Most countries limit foreign ownership, and the same rules don't apply to everyone. So don't believe everything that is told you, even by government officials. Always do extensive research, and get everything in writing, and signed if possible - especially from government officials, the countries rules and regulations regarding foreign ownership, and the names of the people you do business with.

2. Tax, Insurance, and legal implications. One fairly consistent rule in real estate is people are taxed and insured differently depending on the owner's legal status. Many times the tax laws are determined by your legal status ie. natural born citizen, permanent resident, foreigner, citizen by marriage, which region or state you reside in etc. You may pay the same amount for the property as a citizen of that state or country, but pay a different tax entirely. Some countries and states even require that you purchase different insurance on the property. So remember it may sound like a great deal, but after you factor in taxes, insurance and legal obligations, it could be a very bad deal.

3.Location, Location, Location. It may sound like an overused cliché, but it is true none the less. For some reason people just love to own property that directly borders water. A property right on the beach or lake can go for many times more than one down the street, or even just across the street. A house with an ocean or mountain-view could sell quite a bit higher than the next door property that doesn't. Any piece of land or building that has a location more suitable for the intended purpose of the zoning like –corner lots which provide more driveway access for a commercial property, single or multi-family residential buildings near colleges that have high traffic, residential land in higher income areas or that borders parks or limited access areas, agricultural properties near water sources or in high sunlight areas, and even an industrial facilities closer to expandable utility access can be very expensive than those which don't.

DO I NEED A REALTOR?

The most common way to buy or sell is to find a realtor (also called an agent). The amount and who pays the realtors fee changes region to region, and country to country. Typically the fee is split 50-50 between the buyer and sellers agent. Generally it's the seller who pays the realtor's fee, so sometimes sellers list and sell the property on their own. If this is the case, than it doesn't cost a buyer to use a realtor, and there typically isn't a contract established before hand, so if you don't like your realtor you can leave. However if you use a realtor to sell your home, than there is a contract that determines how long you have to stay with them, and how much you have to pay them. Generally the amount is 5-6%. There are a few agencies that take 4% but limit the amount of help they give you. The problem with the lower fees is some buyers agents will not show clients property where there potential fee is limited to 1-2%. Realtors buy-in-large are worth the effort, since a good agent will increase the time and likelihood of your property selling, or you buying the right property.

HOW DO I FIND A "GOOD" REALTOR?

Realtors can pretty much be found everywhere, but good ones are not. Remember it's fairly easy to become a realtor and usually only require a few weeks or months of training. Here are four things to look for:

1. Make sure they work full time, and have been in the industry for a while. There are many who work part time, have just started, or have jobs "on the side". However, one must remember this, "if

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they were any good at what they do, they wouldn't have to work at another job on the side".

2. Make sure the realtor has experience and works with a reputable agency. It is important that the realtor you choose have experience in both the location (region) you want, and the kind (residential, multi-family, commercial) you want. It is also important to make sure the realtor, and agency is reputable. This can be done by calling the local realtors association, checking out the Better Business Bureau, Department of Commerce and Consumer Affairs, looking up references, and going online to research the current and past activities of the company.

3. Make sure the realtor has in writing what they do for their clients. If the agent is too lazy to put things in writing, and only verbally tells you what they are going to do, than you had better find another realtor. Most realtors should at least make sure you are listed on some type of (MLS) Multiple Listing Service, LoopNet (more for multi-family and commercial properties), their own website, and various other online advertisements. This ensures both realtors and individuals can find out the basic information about your property. The other things they should do is put up appropriate signage and informational boxes on the property, place advertisements in the local papers or magazines, put the property on local realtor drive-bys so other agents can see and show the property, open houses for the general public, and place advertisements on free sites like Craigslist, bulletin boards, partner realtor sites etc.

4 Make sure they are willing to list the selling or buying price at you are comfortable with. This does not mean that we can put any price on a property, and we should be willing to listen to the expertise of the individual. Work with your realtor to determine what price you want the listing contract, or buying contract to be, and how much you are willing to negotiate. However in the end you have to live with the consequences and not them.

I HEAR THE TERM ESCROW ALL THE TIME, WHAT IS ESCROW?

When we talk about escrow we are basically talking about the entire process of buying and selling a piece of property. Rarely will an individual buy or sell a property without help from others. The name we give companies that handle all the transactions is called an escrow company (sometimes called title companies). When someone makes an offer on a piece of property they usually put a certain amount of money into an escrow account to begin the transaction. Then the escrow company will handle all the monetary transactions including researching who actually owns the property, are the taxes paid, is there any governmental actions against the property, and basically ensure that all bills and fees are paid at the end of the transactions. One of the most important services for buyers is to ensure that in the end they really own the property, and for the price agreed on. The escrow is kind of like a middle man that makes sure everything goes fairly and smoothly.

HOW DO I KNOW IF THE PROPERTY IT S GOOD DEAL, AND WHAT IS AN APPRAISAL?

There is no one thing that makes something a good deal. A low price doesn't make a property a good deal, if the property has many problems. A great property at a low pricedoesn't make it a good deal if the taxes, insurance, and maintenance fees eat into your living expense or inhibits any profit or income. Even if a property has a high appraisal value it doesn't mean it's a good deal, because the appraisal is not necessary proof positive of the actual value of a property.

This is because an appraiser basically determines an appraisal. The appraiser visits the property to evaluate the condition, type, amount of rooms, kitchens etc, and overall size of the buildings. They then return to research and compare that property to other properties nearby, and what they have recently sold for (within the past 3 months). They then put together a report with some photos, measurements, basic overview of the property, and a list of other properties sold or even for sale in the general area. A price is then set on what your building and property should be worth, when compared to the others in your area.

Of course this is somewhat subjective, because comparative properties may have been sold high or low for another reason, and the appraiser can set a higher or lower value determined by their own reasons. Sometimes the notes and explanation for the property's value may not even be accurate. However most banks will use the appraised value to determine how much they are willing to loan you. Ultimately in the end, you have to determine what you want and what you are willing to pay for it to determine what is a good value to you.

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WHAT IS A HOME OR BUILDING INSPECTION (SOMETIMES CALLED AN ASSESSMENT)?

A home inspection is not typically required by a bank or as part of escrow, but is a good idea. A home inspector is usually hired by the buyer to determine the overall condition of a home and to point out safety concerns with a structure (not environmental concerns). The inspector is a generalist (not code inspector) who performs a site visit, and then puts together a written report. A buyer can attend and walk along with the inspector, or come at the end if they choose. The inspection basically covers the structure, roof, electrical, plumbing, HVAC, interior, exterior and basic site work of the home. They may or may not provide recommendations, and most will not try to persuade you to buy or not buy the home. They are hired to basically provide overall assessment on the basic condition of the visible components on the home.

A commercial building inspection is typically done on certain parts of a building that the potential buyer or seller is concerned with. Sometimes they include all the exterior, interior and site work. Other times they might include only the exterior, or roof, or electrical components. These may also include recommendations for repair, quotes on financial costs for repairs, potential safety concerns, conformance to various codes etc.

IS A HOME CONSIDERED AN ASSET OR LIABILITY, AND IS IT A GOOD IDEA TO OWN A HOME?

The answer to this is not so straightforward, and may be either or both. The reason for this is that if you have a mortgage and make payments, it goes on your taxes as a liability. However everyone needs to eat and sleep somewhere and it's nice not to have to pay for someone else's mortgage through rent. You can also build up equity in the home you own, which can help you with extra cash that you can invest elsewhere. If you do not have a mortgage, and own the property outright than its stated as an asset, because it has value, and may even be worth more than you paid for it. So the answer is, it depends on who really owns it (you or the bank), how much you paid for it, and how much it's worth.

As far as being a good idea to own a home, it kind of depends on what you own, where it is located, and how much it costs to rent a house. If you buy a house in need of allot of repairs, in a lousy neighborhood, paid a high price for it, and have to drive a long way to work and back, than its a probably a lousy idea to own that house. However, if you are near your work, get a good price, for a decent house, in a good neighborhood, than it's probably a good idea to own that house. Also if rent is so low in the area you want to live, than it's probably a good idea to save on the mortgage payments, and put your money to work elsewhere.

WHAT DOES IT MEAN TO REFINANCE, WHAT GOOD DOES IT DO, AND WHAT IS UNDERWATER?

To refinance something means to go back to your lending institute to try to change the conditions of the loan. The good thing about refinancing is you may be able to lower your monthly payments, get more cash out of the loan, or change the length of the loan to best suit your long term objectives. The problem with a refinance is they usually cost thousands of dollars to process, and puts you farther into debt. The term underwater means that the loan amount is greater than the value of the property, and that the owner may not be able to keep making the payments. Let's look at all three reasons why people refinance.

1. Changing the length of time. The longer you take to pay off the loan, the lower your monthly payments will be. However the more you pay in interest in the long run. Many do this to help them afford the home they live in, because now the monthly payments are lower.

2. Changing the amount you borrow. This can only be done if the banks send out their appraiser, to determine if the current value is higher than what you owe on the property (called equity). If the difference is significant, than a bank may loan you up to 80% of the difference in value. For example if you owe $100,000 on a home, but it's appraised at $200,000, the bank may loan you up $80,000 in cash on top of your current loan. The bank will also add the processing fee (often up to 10% of the cash amount) on top of this figure, and then change the amount you owe each month (or lengthen the terms of the loan). This may be a good way to get extra cash, but has also caused many problems and forced people to lose their homes later on. The reason for this is people will spend this new money foolishly, and then not be able to afford the higher mortgage payments a few years down the road.

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3. Lower your monthly payments. This does not mean the bank lowers the amount you owe; it just means they either make the length of time longer, or by lowering the interest rate on the loan. By making the loan term longer, they can lower the monthly payments, and stretch out the amount of time needed to pay off the loan. This has allowed people not to have to go into foreclosure, but the bank makes more in fees and interest in the long run. The other way is to lower the interest rate. If you lower the interest rate on a loan, the monthly payments decrease, because most of your monthly payments go to just pay off the interest. With the interest lower, the overall cost of the loan decreases, as does the monthly payments. Now obviously the best deal for the bank is a longer loan, but sometimes you can renegotiate both, because it's better for the bank to have you making payments than to go through a foreclosure.

I HEAR TALK ABOUT FORECLOSURES AND SHORT SALES, WHAT DO THESE MEAN?

A foreclosure is when a bank or lending institute takes back a property when someone is unable or unwilling to make the payments on their mortgage. This process is called foreclosure, and typically will not start until someone is 3 months behind on payments. When it comes to real estate the truth is banks technically own most properties. When you get a loan on a property, car, or other large purchase, the bank keeps the ownership papers, which they sign over to you when you finish paying the loan. If you stop making payments, the bank has the right to take ownership of the property. The laws change state-to-state, and country-to-country, and some states allow the bank to come after the previous owner for the balance of what is owned after the property is resold. The foreclosure typically takes a few months, to a few years to complete.

Some institutes will work with you to refinance, or to change the conditions of your loan to help you make your payments. When a property is foreclosed on the bank will typically try to sell it right away, and list the property as a "bank owned" property. A short sale is when a previous owner can sell the property before it's foreclosed on. This allows the bank to sell the property, while the owner is released from the obligations of a legal foreclosure (which goes on their financial records). The problem with the term short-sale is a short-sale can take a long time to process. This is because different, more complex rules apply to short sales which include - the previous owner or renter may still live in the property, the bank has to decide if they want to sell to the new buyer at a lower price, new buyer has to process many legal documents and prove they can afford the property etc.

HOW DO I MAKE MONEYON REAL ESTATE?

If you purchase property as an investment, you can make money by selling a property for more than you bought it. You can also make money by renting or leasing the property to others. However you must take into account the amount of money spent in taxes, insurance, maintenance, management and buying and selling fees involved in the process. This is called cash flow. The way you make money is for this to be positive, meaning you take in more in rent than you spend in expenses. The break down basically includes.

Income: Money brought in by renters, or by the amount of money made through various lease agreements. There is also equity that can be derived from the property, over time, if the value increases above the original purchase price. If the price increase is substantial enough, one can obtain a loan, on this value, from the bank or mortgage company. If you use this money foolishly it will just put you farther into debt. However, if you invest this money wisely, like purchasing another property, you may be able to increase your income through this new investment.

Down payments: The down payment is the amount of money you have to pay to purchase a property. This amount typically ranges from 10 – 30%. The rest can be covered by a loan.

Mortgage payments: A mortgage is the amount you own a bank or lending institute that loaned you the money to buy the property.

Interest payments: The interest payments are the amount of money that goes to pay the interest on the loan. The amount you borrow is called the principal, and both are included in the monthly mortgage amount. In the beginning most of your payment goes into the interest, later in the loan more goes into the actual loan. So the sooner you pay off the loan the less you pay in interest.

Price paid for the property: The price includes all the fees and service charges paid during the process of purchasing a property. If you paid cash for a property than you will not have to pay a

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mortgage, or mandatory insurance, and can save a ton of money. However since many interest payments on loans is tax deductible it may be better to get a loan depending on your situation.

Taxes: Taxes on real estate are generally referred to as property tax. The amount is usually derived out of charging a certain percentage of what the property is worth. Each area has a different formula, and some states have extremely high property tax, and can be higher than insurance and management fees combined. There is also capital gains tax charged on the profit you make after you sell a property it held for more than two years. For a primary residence after two years there is no capital gains tax.

Insurance fees: If you have a loan from a bank, than they will require you to purchase and maintain insurance on the property. Usually it involves casualty and general liability like fire, flood, earthquake, tsunami, hurricane, personal injury etc. There is also mortgage insurance, which covers your mortgages if you can't make the payments. It often various region to region, and the amount may change on what the property is worth, location, kind of property, and what is required by law. If you paid for the property with cash, than it's usually left up to your own discretion as to what kind of insurance you need to purchase.

Management fees: When you have an investment property someone has to manage it. If you do not know how, or do not live near the property, than you will have to pay for someone to manage the property. This typically includes hiring someone, or some company to find and keep renters, deal with complaints, find maintenance people for upkeep and repairs, handling paperwork and helping with taxes and insurance. The fee generally ranges from 8 – 15% of the income generated by those paying rent.

Maintenance fees: These basically include everything to keep the property in good shape and rentable. For residential it runs about 12 - 15%, and for commercial property it can run 18-22% of amount of money brought in each year in income. Of course this is just an estimated figure and it is itemized out over the life of the property. When you buy a condominium or townhouse there is a monthly fee that all unit owners pay, which covers most of the exterior, landscaping, site work, parking etc.

In Conclusion:

It may all sound like allot of work, and it is. Although if you don't handle stress well, and shy away from complicated transactions, than you might look into another form of investment. As in every transaction, the above items might not all apply, but most will be a part of the process. If they are, each needs to be included in the decision to purchase real estate as an investment. If you already own a property, than here is what you can do to determine if you are cash flow positive. If you do not own a property yet, but want to, than you have to try to find out what each may cost you. You can do this by researching past history of the area, how much rent is nearby, what kind of utility costs there are, how are property taxes charged, what kind of loans are available, etc.

To find out if a property has good cash flow, just add up all the items above in an expense column, and minus the total from how much the property brings in over the year. This figure will give you a good idea on how the property is as an investment or on which areas you can change to make the property a good investment (typically by trying to negotiate lower taxes, cheaper insurance, lower maintenance fees etc.) Remember that it's best to run these figures out over a period of time, say at least 3-5 years. You can also check to see what other similar properties are selling for, and see if the value is increasing or decreasing. This way you can get a feel for how much the property is making, or loosing, and whether the property has a chance to increase in value over the time you want to keep it.

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