

# Flipping Houses

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## ***Good Investment?***

The hottest investment going these days is flipping property. Investors are making huge profits buying luxury properties before they are finished and then selling at a profit before actually taking possession. Most make more moderate profits buying distressed property and improving it.

Experts disagree on how safe an investment flipping is. Economist Tucker Hart Adams claims that this practice has created a housing price bubble by artificially inflating property values. She says that the bubble must pop. Other experts claim that even if the market in places like San Jose, CA and Miami, FL have been grossly inflated and may be at risk, the Denver market will be relatively unaffected because the market inflation here has been small.

Adams says, “By the time your hairdresser is flipping properties and the grocery clerk is giving real estate advice, it’s too late to get in the market.” Others say that you can make money if you adjust for the present market. For example, middle class homes in the Denver area are selling slowly now. The market for these homes seems to be declining. Some experts believe that opportunities are still plentiful in the thriving high-end home market. They say low-end market presents more opportunities as it becomes harder to buy homes due to rising interest rates and declining middle class income and jobs.

## ***What is Flipping?***

There are two basic ways to flip property. One is to buy with the intent to resell at a profit without ever occupying it. The more common method in the Denver area is the fix and flip. The principle is simple, acquire a property, remodel/renovate and sell at a profit.

The fix and flip works in most markets. There are always distressed properties on the market. The profit comes from improvement of property and/or from market appreciation.

Not everyone makes money. Some people do take big loses. Check out this article by, George W. Mantor, known as the "Real Estate Professor," [http://realtimes.com/rtapages/20050930\\_flippers.htm](http://realtimes.com/rtapages/20050930_flippers.htm)

Mantor says a common way to make money flipping is to buy houses in foreclosure. He says, "Let's be very clear, when you target homeowners in distress, your intention is to defraud them of the equity that is rightfully theirs. It isn't illegal, but it does require manipulation and deceit. The only reason a seller in distress would decline to receive full market value for their property is if they didn't know what the true market value was." There are many other ways to acquire property.

The fix and flip is attractive to small investors with little or no experience. One hundred percent plus financing makes it an easy investment for many people to get into. Stories about quick wealth flipping are everywhere. An abundance of workshops, seminars and books claim, "You can't fail if you follow our method."

### ***Good Planning is Essential***

The profit is there to be made by even the novice, but planning is essential. Investors who go into projects blindly are probably going to lose. Cost must be accurately projected at the beginning of the project. The number one rule of remodeling and renovation is that there will always be surprises. Actual costs are so hard to estimate that Russ Berget, who has over 30 years experience fixing and flipping in the Denver area, says the he still comes in over budget almost every time.

Berget says common mistakes, besides not expecting the unexpected, are underestimating cost to hold the property until sold and cost to sell the property. Timelines are difficult to keep in a constantly changing market when dealing with properties that can hold costly surprises. It usually takes longer to fix and resell than anticipated.

Be realistic and work with a good real estate agent who can help you understand the present market conditions in the neighborhood where your property is. He/she can help you decide the level of renovation that the neighborhood and market merits. He/she is also a great resource for deciding how to configure the property for maximum profit. A knowledgeable agent can help determine the proper price for the neighborhood. Consult with him/her before making plans for renovation and marketing.

Each property is unique and will have unique problems. You never know what you'll encounter when you open a wall or pull up a floor. Berget says one of the biggest mistakes investors make is not knowing what they are getting into. He suggests that flippers need to plan on doing as much of the work on the property themselves. Contractors eat profit, but trying to do work beyond your skills and knowledge can consume all profits as well as your enthusiasm. Accept your limits.

The surprise expense of removing asbestos, lead or mold can destroy hopes of making a profit. Polybutylene, galvanized or lead plumbing, defective furnaces, roofs or

foundations are defects the average investor may be unaware of. Minimize the surprises by getting a good inspection before buying.

A good inspector will find most defects and be able to identify potential problems. Hidden defects can be impossible to identify, but most hidden defects reveal themselves in visible clues. Many flippers buy without an inspection. This small expense can make the difference between profit and loss.

### ***Acquiring property***

There are many ways to acquire property. Foreclosures and buying off the open market are common. Loans are readily available to help investors flip and fix with a minimum of up front cash. Good, lasting relations with lenders depend on things going according to plan. Remodels seldom go according to plan. Regardless of how you finance, your plan needs to be complete, budgeting for every contention including the unexpected.

Russ Berget suggests at least 6 months in carrying cost in reserve. He suggests using as much lender money as possible keeping cash reserves back to cover the unexpected. Try for 100% + financing to cover acquisition and fix and flip costs. Lenders are lending on the finished value of the property, not the present value. They loan money based on your track record and their belief in your ability to successfully complete the project. Once you develop a good track record, borrowing full costs becomes easier. Use a lender that specializes in fix and flip.

Remember that ARM is Adjustable Rate Mortgage and the payments go up if interest rates rise. Plan for increasing payments if you opt for these plans. Watch out for prepay penalties.

An increasingly popular approach to fix and flip is to find a homeowner who is the position of losing his/her home. By creating a partnership with the homeowner, investment is minimized.

The investor puts up money to bring loans current and to remodel/renovate the property. The profit is split between owner and investor. The homeowner gets another chance and possibly provides some labor. The investor gets a deal that doesn't eat money as quickly and requires less capital. Investors doing this claim they never lose money.

The present market in the neighborhood of the property you are considering determines what is and is not a good investment. It's easy to buy property in an area where jobs are disappearing. This hard part is selling the property in this market.

In a hot market, you may buy a property and sell it within a few days for a profit. This occurs in an area where jobs are growing quickly or in luxury markets. Water front condos in Miami have been hot investments that yield huge profits without ever taking possession of the property. Perhaps an extreme hurricane season will slow this market. Value is always the perceived value of the buyer. If fear rules the market will slide.

In a hot market, it may be hard to make a buying mistake. In most markets, profits are harder to make. Real value must be added to the property to reap a profit. In these markets, buying decisions must be made more carefully. Conventional wisdom is to buy the worst property in the best neighborhood possible.

Russ Berget, says the biggest mistake investors make is not having enough equity potential in the deal. He suggests that a minimum of \$30,000 must be possible to cover the expenses and allow a profit.

After making initial estimates on all cost to buy, fix and sell a property you can project a tentative sales price. Berget recommends the selling price be in the middle of the neighborhood range and slightly under market value. It should also be in the middle of the MLS price bracket it appears in online.

Time consumes money in these deals. The property must sell quickly, or be taken off the market and rented. This is sometimes desirable to allow equity to build. If you don't have enough equity to make selling profitable this may be your best plan. You will have to prepare the property for market again. Anticipate this cost.

In a luxury market, the best properties may be the better deal. In Aspen, all real estate, no matter how grand, or how average, has traditionally appreciated at a faster pace than in Denver. The most expensive homes sell quickly and provide the greatest leverage. All value is perceived value.

### ***Renovation Plan***

Determine the level of upgrading the property warrants. If you are in a million dollar neighborhood, home theatres and wine cellars may be assets. In a \$150,000 home they are wasted investment.

Most people are proud of their work and try to do the best job possible. Flippers may envision their dream homes and try to create this in their renovations. Flipping is a business and must be approached as such if it is to be profitable. The level of improvement should be the minimum it takes to bring the property to the condition of those in the neighborhood.

This doesn't mean taking shortcuts that ignore issues that will return to plague new owners. Covering up problems may be tempting. It is done. Mold, water damage, insect infestation, lead paint and asbestos may be simply ignored or improperly covered. Covering lead paint and asbestos may be the acceptable remediation in some cases, but covering mold, water damage or insect infestation is never acceptable.

Systems problems like cracked heat exchangers, gas leaks, galvanized, lead or PB plumbing or aluminum wiring may be overlooked. In most cases, a buyer's inspection is going to reveal these things. You are likely to have to adjust the selling price to cover

these repairs and lose some of the value of remodel. All value is perceived and doubts about the quality of workmanship decrease value. In a hot market, you may get away with selling to an anxious buyer without an inspection, but it's dishonest and will not serve you in the long run.

If you don't have the expertise to recognize and correct defects, get a professional. In all cases, if you are unskilled, use professionals for HVAC, electrical and plumbing upgrades and repairs. Consult an engineer when changing structural components. If a potential for danger, or recurrence of the problem, exists, get professional help.

In flipping, time is money. Not only should you anticipate going over budget, you can also count on finishing late. It's part of the game. Your schedule may be at the mercy of contractors, code inspectors, lenders or government agencies. Most of us are overconfident and believe we can do things quicker than we actually can. Figure generous extra time for your own tasks.

Get bids on work to be contracted, along with time estimates. Work must progress in the proper sequence. Ask contractors where they need to fit into the schedule if you're not sure. Some work can be done simultaneously. Demolition must be completed before reconstruction. Demolition time and cost can't be overlooked or underestimated. Plumbers and electricians may work well at the same time, but flooring contractors and painters don't mix.

Itemize all permits, materials, systems and appliances you'll need. You can often save money looking for bargains. You can also lose more time than it's worth.

Double the amount of time you plan to take to finish the project and sell the property. Be certain you have the money to carry the project for this long.

Start thinking about marketing before you acquire the property. Never show the property until it's done, but begin planning. The renovation plan should be steered toward what it takes to make the property the most marketable. All remodel and repair should be tailored to the tastes and means of the people who will live there.

There are many books, television programs, videos and web resources for staging a house for sale. From curb appeal to the feeling in each room, every aspect needs to be considered before starting. The better the house shows, the quicker it sells. Tend to all details.

### ***Selling Your Property***

It can be tempting to sell your property yourself. A very hot market might make this a good plan. If buyers are actively combing the streets looking for any house for sale, acting as your own agent may make sense. In most markets, a professional real estate agent is best.

You need current knowledge of the neighborhood sales and general market you're working with. The advice you receive for acquisition, remodel and preparation for sale are invaluable.

When you sell, it's important to price your property right the first time. If it doesn't sell quickly, it can be pushed into a buyers already rejected file. The property becomes market weary. Even if the price or terms are sweetened, it probably won't get a second look. Professional agents know what actions to take and when so buyers will give you a new look.

There is money to be made flipping property. Russ Berget has proved this for 33 years in all kinds of real estate markets in the Denver area. I asked if he had ever lost money on a deal. I expected an immediate, "Of course." His reply surprised me. He said he must have lost money on some deal, at some time, but he couldn't think of one.

Planning and hard work will build wealth steadily over time. George W. Mantor, the "Real Estate Professor," says it is not a way to quick wealth. He suggests that lottery tickets are a better plan with more manageable costs.