https://www.spousesflippinghouses.com

Hosted by: Doug & Andrea Van Soest

Episode 27 – Wholesaling Explained! The "How to" of One of Our Favorite Investing Strategies

Andrea: Welcome back to Spouses Flipping Houses Episode 27. Today we are talking about one of our favorite subjects.

Doug: Yes it is.

Andrea: Wholesaling.

Doug: One of our favorite strategies, especially right now, wholesaling.

Andrea: Everybody knows what it means to flip a house; everybody knows what it means to be a landlord and keep a rental, for the most part, but not everybody knows or quite understands what it means to wholesale.

Doug: Yeah and it can be a great strategy, even if you're not a wholesaler as your main strategy, it's good to know this and utilize it when you need it or at least understand the process if you're going to be buying properties from wholesalers, that kind of thing. Excited to get into that later. But before that, what's happening in our rehabs this week?

Andrea: A lot! We got a couple that are almost finished and this is my favorite stage, when the cabinets are going in. I feel like when it comes down to the finish line, everything happens so fast, and it's really fun. That's when it gets really exciting. The cabinets go in, the tile, the bathroom deco tiles, all that sort of thing, the fixtures are all kind of going in at one time, and it's so exciting.

We've got two or three that are in that same stage right now, and so I can't wait to drive around tomorrow and check them all out.

Doug: Yeah finally. These are some big projects and kind of when they transform from a construction project to a house, so it's exciting to see that.

Andrea: And then we're starting up another rehab actually in our own town of Marietta. Believe it or not, in the last eight years, we've flipped a lot a lot a lot of houses, and this is only the second one that we have done in our hometown, so that's kind of fun.

Doug: Yeah for whatever reason we just haven't been able to land projects we wanted to do here that the numbers seemed to work, but this one is five minutes away. So it's pretty cool, pretty exciting to start that. I like the convenience factor.

Andrea: Yeah super convenient, and then you and I kind of went back and forth on this one a lot as far as what we were going to do to it because we wanted to keep our budget small so it could be just a quick rehab, turn it around, put it back on the market. It's in a great neighborhood that people want to live in, so the reality is we don't have to do a whole lot to it.

But the house is full of popcorn ceilings, and I felt like that was completely unacceptable.

Doug: Well you know, a lot of the houses around here are newer-ish. So this was built in the late 80s, which is actually one of the older homes in our area because we're just a bunch of new track homes. So there's not a lot majorly wrong with these houses other than they're typically dater, and they have popcorn ceilings, and they have obviously old appliances and stuff that we would want to upgrade.

But I'm thinking, *Man, we're just going to put this thing right back on the market. There's lots of homes just like it. We can sell this thing for the market value and not have to put a lot of money into.* But once we get in there, we always want to improve the house.

Andrea: Yeah, it always, and I think we've said this before, it always needs at the bare minimum, probably paint and carpet. Just to feel fresh, and clean, and new.

Doug: Yeah definitely.

Andrea: But this one had the popcorn ceilings that were just more chunky than your normal popcorn ceilings. It just felt so much worse.

Doug: Chunky popcorn.

Andrea: Well you know it's kind of chunky.

Doug: Maybe it was kettle corn ceiling.

Andrea: It's like cottage cheese has been tossed up there and stuck. It's so ugly.

Doug: It was pretty bumpy, pretty lumpy, and it needs landscaping too. So once you get into it, it really needs more than I thought, but still. It's a minor rehab on the scale of the rehabs that we typically do.

Andrea: Yeah we'll still be able to do it really fast, and I won. Woo-woo! We're scraping the ceilings.

Doug: Chalk another one up for Andrea there in the win column.

Andrea: It's going to look really good though. I think you'll be glad.

Doug: No, yeah. So that one's coming up too. Well before we get into our main topic we wanted to encourage you again, if you haven't visited our website, please do that.

SpousesFlippingHouses.com, there's a free gift for you there if you haven't received that.

We have some before-and-after pictures. You can listen to our episodes there, leave some comments, and we love getting feedback from the listeners. So please check that out. Also if you haven't subscribed on iTunes, do that and leave us a rating and review. That really helps us out. We really do appreciate the ratings and the feedback on iTunes.

Andrea: On to wholesaling, Doug, what is wholesaling?

Doug: What is wholesaling? Wholesaling is you have a owner of a property, and you negotiate a purchase price. Then, you find another buyer, and you negotiate a sale price for a higher amount and wam-bam, the difference is your wholesale fee. You connect the two, and you get paid the difference.

End of story. Pretty simple, right?

Andrea: Sounds pretty simple.

Doug: Yeah, it's very simple. That's its simplest terms. Now there are many, many ways to structure a wholesale deal. There's not just one-size-fits-all. So, we thought we would talk about four of probably the most common or the most popular ways to do wholesale of property.

And we're going to get into that. Now there are many more, there's other ways, and creative ways, and things like that, but these are the four main ways.

Andrea: Yeah, the first way that you can wholesale a property is to actually use your funds to close on a property from the seller. So you go through the whole escrow process; you close on it in your name.

Doug: You own the property at that point.

Andrea: Yeah, you are the owner. The title is in your name. Then, you go and quickly find a new buyer, whether you quickly put it on the MLS or you put it out there to different buyers that you know of that buy that kind of inventory. And without doing anything to it, you quickly resell it for a profit.

Doug: Correct. That's wholesaling number one.

Andrea: That's kind of "a-to-b-to-c."

Doug: Yeah, so a-to-b, you're being "b." And then b-to-c, "c" being the end buyer at that point.

Andrea: A few things about this method for wholesaling is that number one, you will need money to close on that property or you'll have to borrow money, transactional funding.

Doug: Partner, something.

Andrea: Hard money, whatever it is. So if you don't have your own funds, then you're going to have the cost of money included that's going to come out of your profit.

Another thing you want to think about is that doing this takes a little bit longer.

You have the process that it takes to close on the property that you're buying. Then you have to do your marketing to find a new end buyer, so that just lengthens everything plus all of the escrow time involved.

The last thing you need to know about this is that there's a little bit more risk involved because you are going to be the owner of the house. You will take title; there's expenses and liabilities that come along with that, and then what if you can't find an end buyer at a higher price than what you paid? Well, that's a big fat bummer.

Doug: Too bad for you.

Andrea: Now why would you want to do this? Because we just kind of made it sound like maybe it's not a great strategy, but there are reasons why you would definitely want to close a wholesale deal in this way. And one of the main reasons is to protect a large profit.

So if you have created a very large wholesaling profit for yourself on a particular deal, well, the seller might freak out if they see that on the closing statement or the buyer might freak out if they see that on the closing statement. Should they? No they shouldn't because they're both getting to sell or buy a property that they want to sell or buy, but it's human nature.

Sometimes people will freak out if it's a large wholesale fee that you're going to be earning. So it might be in your best interest to protect that by actually closing on it, and then reselling it, and nobody knows what your profit it. So it's kind of an element of privacy.

Doug: Yeah. The second way or popular way to do a wholesale deal is much simpler, less risk, a lot less moving parts. And it's basically to just take a finder's fee, also known as a referral fee or acquisition fee, and with this method, all you're doing is basically locating a property and letting another buyer know about it, your wholesale buyer, your end buyer.

And they will pay you a fee for that service. You can negotiate any fee you want as long as it's okay with both of you. Sometimes that's paid through the escrow closing process; sometimes it's paid outside of escrow. You're known as what's called a "birddog" in the industry. This is called bird-dogging.

And if you get the visual of a dog retrieving a bird or going to stir up the birds for the hunter, you know it's essentially what you're doing. You're looking for deals for a buyer and then getting paid for that. Be sure you check the laws in your state, because sometimes there could be tricky ways that you want to make sure you're getting paid in a legal manner for the services you're providing if you're not a licensed agent blah blah blah.

We're not attorneys, but anyway. Just check on that stuff, but that's a simple way to do it.

Andrea: Probably the least risky way of starting if you don't have money, right? Because your end buyer will be the one putting in the earnest money deposit. You're not doing any of that.

Doug: Yeah your end buyer typically is going to be the one on the contract as the buyer. The end buyer is the only buyer. You're just sort of assisting that buyer and getting paid a fee for it.

Andrea: Yeah, you basically just found it. You're telling them about it. They're hooking you up.

Doug: Right, so that's method number two, finder's fee.

Andrea: The third method that you can use for wholesaling a property is what we call the double close or the simultaneous close. So in this instance, there will be two escrows that are happening at the same time. So your seller of the property is "a" and you are "b."

So we've got an escrow between "a" and "b," and we have a separate escrow going on at the same time between you and your end buyer, that would be "b" and "c." So you are involved in two escrows at one time. So the end buyer, "c," will be using their money to close the first escrow between "a" and "b."

Doug: Have we lost anybody yet?

Andrea: And so usually these closings would be concurrent. They'd happen at the same time so you're not bringing any money. Your end buyer that you have found is going to be funding the first escrow.

Doug: Yeah. The “c” buyer funds the a-to-b escrow. So it’s really not that complicated, but sometimes you have to wrap your brain around what’s happening. You just have two separate escrows. One closes literally minutes before the other, so they call it simultaneous or a double closing.

And you actually are on title, in the chain of title, for about five minutes or whatever it is. And it’s a-to-b then b-to-c concurrently.

Andrea: And this can be structured in different ways. So maybe your end buyer is supplying the earnest money, maybe you’re the one supplying the earnest money for the first transaction. It can probably be written up in different ways, and this probably varies state to state because…

Doug: It does, I think.

Andrea: Yeah, a lot of escrow companies won’t actually do this type of transaction. Some will, but a lot won’t.

Doug: In our experience in California, most escrow companies don’t do this. It’s just too many moving parts. You really have to have a lot of disclosures, disclose to everybody what’s going on, what you want to do legally. And you know what? Quite honestly, we don’t really like this method because of that.

It’s just too many moving parts. Then you’ve got two escrows, fees, yeah you’ve got all of this different stuff. And it’s just, to me, there are too many things that could go wrong with it. But it is a method that people use.

Andrea: This is another way to keep your profit private from the buyer and seller. So when you've got these two separate transactions, they don't know who is making what. So that's why people do this.

Doug: Yeah, that's why people want to do it, if you have a larger spread typically. The fourth common way to do a wholesale deal, and this is our favorite; it also happens to me in my opinion, one of the simplest ways, and that is just an assignment. Okay, so what are we talking about with an assignment?

Well, you get a contract with a seller, and it's in your name or your company's name, whoever is the buyer. And then all you're going to do is market that contract, you're going to sell your interest in that contract to another buyer, and that's called an assignment. You're actually going to assign the contract to another buyer in escrow, and then collect— you're going to charge to do that, assignment fee, marketing fee, wholesale fee, whatever you want to call it.

So you actually never buy the property in this instance. There's no risk because you're not using your money. You're actually not going to be the buyer. You are on contract, but then you are just selling your position as the buyer to somebody else.

Andrea: However, your profit will be on the closing statement generally.

Doug: For the buyer, it will. You have to have a buyer that understands this process, is okay with whatever fee you make. Because some people, like Andrea mentioned earlier, just weird out if they know you're making a lot of money on a deal, even if it's a great deal for them, they just get funny if they see a big fee there. So that's one risk.

You've got to make sure you're dealing with someone who is okay with you making money doing this deal and obviously is okay with how it's all structured. And also you need to make sure that your contract is assignable, that is says in the contract, "you have the right to assign this contract," which is very, very common.

Most escrow companies totally understand this method and are okay with it, and it's just a simple way to do it. So we really like this method. This is our favorite. And one thing you need to be careful of with this strategy, certain states are a little more harsh on this than others, but in this strategy when you're looking to find a buyer, you want to market the fact that you have a contract to buy the property.

You're not actually marketing the property itself. So if you're putting things out there on the worldwide web, like on Craigslist or however (that's a whole other podcast episode on how to find a buyer), but you just want to make it clear in your advertising that you are selling a contract, not a property. Make sense? Okay good.

Andrea: Yeah, that you're not the owner.

Doug: You're not the owner, correct.

Andrea: Now we did nine wholesale deals in the month of March and every single one of them I believe was this strategy, number four, the assignment of contract.

Doug: Yeah, it's the absolute best way to do it in our opinion, and we are dealing with buyers that we normally deal with that are familiar with this process, and that makes everything easier too.

Andrea: Right. So those are the four types of wholesaling strategies that people generally use. The first one, completely close on the purchase and resell it. The second one, you just take a finder's fee where you're essentially a birddog. The third one is the double or simultaneous close, which you can't always do depending on your escrow company. And the fourth one is the assignment of contract, which is our preferred method of wholesaling.

Doug: Right. So let's just quickly touch on some of the benefits of this strategy of wholesaling.

Andrea: Yeah the first one is that it's basically low risk because even if you do close it and resell it, you're not the one taking on all of the liability of fixing it up and going through that whole process to get it to the finish line. You're making your profit really quick and moving onto the next one.

Doug: Yeah, and it doesn't have to require a lot of money to do this strategy. In fact, it doesn't require any money if you are able to locate properties for free through your network, through the MLS, however you can find properties. It doesn't require a lot of money.

Andrea: It's a good way to start.

Doug: Yeah it's a great way to start.

Andrea; Yeah, the third benefit is the fact that you get paid immediately. When you do a flip, you are taking on this challenge, and you're not going to get paid on it for four to six months, maybe longer— maybe shorter if you're really, really good. But your payday comes much later, so in this strategy you get paid right away.

Doug: Right, and the last thing is you basically can create your own income here. The better you are at finding below market deals, however you go about that, the more money you can make because there is typically a price range that a flipper will pay. And the more you can get the property below that, the better pay you can get. So that's up to you.

Andrea: Now I have a feeling that a lot of people are going to be curious, what is an acceptable profit margin? Or what's an acceptable mark up on wholesale deals?

Doug: Good question. And here's how I've heard that answered in my favorite way by our favorite quoted person Mike Cantu. They say, "Mike, what do you charge typically on a wholesale fee?"

He says, "I charge as much as I can get with still leaving a little meat on the bone for the buyer." So as long as it's a good deal for the buyer, charge as much as you can get. You're in business for a profit. Right?

Andrea: Right.

Doug: So you may hear people answer this with, "Well $5,000 is a standard wholesale fee," and you know what? I wouldn't listen to it. There's no standard wholesale fee in my opinion. I know people who make far less on wholesale fees, people who make far more. It varies quite a bit, so there's no real answer to that.

My opinion is you charge the most you can get for it.

Andrea: It might also depend on your method of marketing and how costly that is to you. So if you're door knocking, you might be totally cool with taking a couple thousand dollar market because it cost you nothing to get that, whereas we are sending out thousands and thousands of mailers.

It's very expensive, so we generally don't like to do a wholesale that's less than $10,000. It just doesn't make sense.

Doug: Yeah because we're spending a lot to get those deals. And the other thought that I just was thinking about is that if you're working with consistent buyers over, and over, and over that are easy to work with and good buyers for you, you want to provide them with a good deal because they're going to be repeat buyers from you.

So if you mark it up so much that you're squeezing their profit out of it, they're not going to buy from you again. So to keep them coming back for more, and more, and more, you definitely want to leave some meat on the bone for them. That's one thought.

Andrea: Yeah, I think that's really, really important actually because this whole business is about creating win-win relationships, whether it's win you're buying a property or especially when you're selling because you do want to have that repeat business.

Doug: Yeah, and if you sell somebody a deal and they end up losing money on it, not only do you feel bad, but they're not going to come to you again for a deal. You've just lost that customer.

Andrea: Yeah they won't trust you.

Doug: Right, so just keep those things in mind. Alright, so we've got five quick tips for you here in regards to wholesaling. When we get a property under contract typically, we just know it's a deal. We don't necessarily know what we're going to do with that deal every time we get it under contract.

We need some time to analyze that, so we may end up buying it, fixing it up, and selling it, the traditional flip that you can think of. We may end up wholesaling that deal. We may end up wanting to keep it as a rental. We don't always know from the very beginning, and sometimes it takes a day or two to analyze the deal and find out what's best for us in that situation.

Andrea: And it may also have to do with what else we have going on at that time. Maybe we have a lot of fix-and-flips going on, and so it's best to just wholesale it.

Doug: It absolutely does which is another good reason if you're a traditional flipper and you come across a deal, it's good to know about this wholesaling strategy because if you're just too busy with all of the projects you have going, you still could possibly make a little profit on a wholesale deal by selling it to another friend of yours who is looking for a deal at that time. So it's a good thing to know.

So the first tip would be to have plan A and then have plan B. We typically go into an escrow, let's say we have an intent to wholesale it. Sometimes, we aren't able to find a buyer for an acceptable fee that we're willing to take for that wholesale deal. Well in those cases, we know that we bought a deal when we got it under contract, and we will go ahead and close on that deal and just flip it ourselves.

So that's what we'll typically do, so just have options. You don't want to just have only one exit strategy and all your eggs are riding in that basket, because what if you can't find a buyer for that? So just be flexible and be willing to do something different.

Andrea: Our second tip for wholesaling is don't string a seller along if you can't find a buyer. This is really important to us. Our reputation is important to us. These sellers are usually in a tough situation in their life, and the last thing they need is for you to string them along when you really can't perform.

So stick to your contingency dates and perform according to the contract that you agreed upon as best you can. If you can't, let them know right away so they can move along and figure out another solution to their problem.

Doug: Right, good tip. The third tip would be to disclose in your contract what you intend to do. We have a disclosure in our contract, and it should say something to the effect of, "the buyer is an investor and intends to rent, sell, assign, or joint-venture with other partners for a profit."

Typically they're going to know up front that you're an investor but in the event that they don't, you're making clear that you're looking to do this deal for a profit, and you're listing several ways that could happen, which is, in our case, very accurate because we don't always know what we're going to do with the property. We just know that we intend to make money on it somehow. So definitely put that disclosure in your contract.

Andrea: The fourth wholesaling tip is to get a nonrefundable deposit from your wholesale buyer or your end buyer along with your signed contract or agreement with them, just in case they back out.

Doug: Yeah, you don't want your money to be on the line if they fail to perform. At least you have their earnest money deposit that you can give to the seller because you failed to perform on the contract.

So tip number five, just know that it's okay to make money doing this. The wholesale world exists not just in real estate of course but all products. You have middlemen who sell at a wholesale price to the grocery stores, or Target, or whoever that then sells at a retail price. That is what you're doing in this business, and it's okay to make a profit doing it.

Andrea: Yeah, you are providing a service. You're providing a service to the seller, and you're providing a service to the buyer. If seller A knew how to find buyer C, they would just do that, but they don't, and you do. You know how to find seller A, and you know how to find buyer C, and you connect the dots. So you're providing a service, don't feel bad about it.

Doug: Absolutely, absolutely. So that's wholesaling in a nutshell. Great strategy, one of our favorites. We do love the fix-and-flip. That's like our bread and butter. We love to take a house and turn it into something beautiful, and that can generate a great profit for you, but this is another great strategy to have in your toolbox so to speak.

So we hope you got a lot out of this episode.

Andrea: Coming up really soon here, we're going to have another question and answer episode. I have a feeling that this podcast episode may have generated several more questions.

Doug: Hope so.

Andrea: So feel free to send us your questions at andrea@spousesflippinghouses.com. We will definitely answer your questions via email, and we may read it on the next podcast and answer it for everyone.

Doug: Yeah, so send in those questions and until then, I guess we will just talk to you next week.

Andrea: Have a good week.