



LENDER INFORMATION

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TABLE OF CONTENTS

Item #1: Your LTV should be a maximum of 70%.....	4
Item #2: Loan Review and Monitoring.....	4
Item #3: Title Insurance.....	4-5
Item #4: Close with a Professional.....	6
Item #5: Comparative Market Analysis.....	6
Item #6: Fire Insurance.....	7
Item #7: Always Have the Borrower Sign Personally.....	7-8
Item #8: Your Rights in Case of Default.....	8
Item #9: Repairs.....	8-9
Item #10: Second Mortgages.....	9
Item #11: Never Make Out a Check Directly to the Borrower.....	9
Item #12: Assignments of Rents.....	9
Item #13: Default Steps.....	10

“Everything You Need To Know About Lending Out Your Own Money”

When it comes to lending your money on a real estate transaction, there are important items that you must require with respect to your transaction, in order to be profitable, successful and for your investment to be safe. This report covers 13 essential items, in detail

Item #1: Your LTV should be a maximum of 70%

The Loan-To-Value (LTV) Ratio is the ratio of money that is borrowed vs fair market value. Residential mortgage loans from banks traditionally have a maximum LTV of 80% (for example, an \$80,000 loan on a \$100,000 home). But when lending your personal funds, the LTV must be lower to protect your investment.

You should aim for a 65% -70% LTV. A high LTV loan creates risk with little or no profit due to over-leveraging the property.

To maximize your success, you must maintain a reasonable risk factor, where you will require a maximum LTV limit of 70%.

Item #2: Loan Review and Monitoring

To be certain that your loans are secure you should perform a periodic quality analysis for the purpose of reviewing and monitoring the loan, as well as your overall portfolio.

To accomplish this, perform a visual inspection of the property in person or request photographs of the work in progress from the borrower. This is typically agreed upon prior to closing. A portion of the renovation proceeds is held in escrow. Once the project is 50% completed, the balance of the escrowed funds are released.

Item #3: Title Insurance

Title Insurance will not cost you anything, as the borrower bears the cost of this insurance. Upon completion of a title search, the title insurance agent will then issue title insurance, guaranteeing that no errors were made in the title search and that there are no errors in the public records. Title insurance also protects against undisclosed title defects, that no matter how thorough, extensive, and exacting a search is made; it is still possible that hidden risks remain. Title insurance protects you against title problems that may subsequently surface, as some of these defects may not appear until many months or years after a property is sold. Without which the end result could be the loss of the property, expensive lawsuits, and delayed closings. Title Insurance protects against public records that have been searched that may not reflect the following.

- Forged signatures, fraud, or duress in obtaining signatures
- False impersonation
- Instruments executed under expired, revoked, or false powers of attorney
- Delivery of a conveyance after the death of a grantor
- Homestead rights of a spouse
- Undisclosed heirs and improperly probated wills
- Deeds by minors or persons of unsound mind
- Deeds by a corporation without proper legal authority
- Misrepresentation of marital status
- Clerical errors in recording legal documents
- Survey errors
- Mistaken interpretation of wills and trusts

An insured title protects against an attack on the title of the rights of the insured. Title insurance ensures that you have a marketable title to the property and if any problems are found, the insurance company will pay all costs. Any loss as a result of the above defects is paid up to the limits defined in the title policy.

A one-time premium is paid for this insurance, transferring the risk to the insurance company so that the real estate is as it is stated to be in the policy. This is important since the title insurance policy is what indemnifies the buyer and/or the lender against losses that may be incurred if the title of the property is not what is stated by the policy. The borrower pays for this coverage for you.

Title insurance is not a title search. It is the title insurance that “insures” that all searches with regard to the property are accurate.

There are two types of title insurance:

1. Owner’s Coverage. This protects the property owner from defects in title that could affect the property’s marketability.
2. Lender’s Coverage. This type of coverage insures you, the lender, against defects to the title. In case you become the owner of the property due to a foreclosure upon the loan, this will protect you. The closing agent should physically make you a lender’s policy within 3 weeks of the closing.

Title insurance is a protection in case inaccuracies should occur involving the title and what is stated on the policy. It provides both the purchaser and you, the lender, with comprehensive, no-fault protection against the risks, which are inherent to real estate dealings.

The advantages to you when the borrower purchases title insurance for you include:

- No-fault recovery of losses
- The payment of all related claim costs
- Broad coverage including title defects resulting from negligence of the lawyer
- A reasonable one-time premium
- Flexibility to arrange special program coverage not available elsewhere in the market.

You will receive coverage for the validity and enforceability of your security investment.

Item #4: Close with a Professional

Closing with a professional will not cost you anything, as the borrower bears the cost of this service. It will give you invaluable peace of mind because you will be assured that the required documents are properly recorded. With the assistance of a professional, the risk of the transaction has been reduced immeasurably increasing your potential for a successful, profitable deal.

Item #5: Comparative Market Analysis

A professional market analysis should be required of your borrowers before you agree to lend to them. A Comparative Market Analysis is a written estimate of the fair market value of a property made by a qualified realtor, based upon available facts and a thorough inspection of the property being purchased. There are many reasons for this, and it is up to the borrower to have this analysis completed. It is completely free for you.

By having a market analysis done, you'll have access to essential facts with regard to the property. The facts will make both you and the borrower well-equipped to handle the investment. The analysis should be "after-repaired" value

In addition, an analysis will forewarn you both of any potential issues and validate the loan-to-value ratio described above. In essence, this serves to protect you by ensuring that you are not lending more money than the fair market value of the secured real property.

Item #6: Fire Insurance

Fire Insurance will not cost you anything, as the borrower bears the cost of this insurance. Fire insurance should be considered absolutely necessary for real estate transactions. In general, a fire insurance policy will protect you in the event of loss or damage to the property if it was a result of some (or all) of the following events:

- Fire
- Lightning
- Explosion
- Earthquake
- Impact
- Collision
- Riot
- Theft and malicious acts

Fire insurance will normally cover a number of elements of the property, including:

- Kitchen fittings and appliances
- Outbuildings
- Garages
- Paths
- Fences and gates
- Site clearance
- Swimming pools (which includes the equipment for heating and filtration)
- Fees for architects, engineers, and/or surveyors

A loan should never be closed without fire insurance, and a 6-month premium should be paid at closing time.

You are listed on the insurance policy as the mortgagee. Should the insurance expire, you may force the activation of insurance, maintain the coverage, and charge the borrower. The only way that you could lose is if the property burns down and you haven't any insurance.

Item #7: Always Have the Borrower Sign Personally

When making a loan, you should always have the borrower sign personally on the promissory note. In addition, you will also want to include the signature of the trustee, if the property is in a trust.

There are many ways to take title to a property. The owner can take title personally or they could take title by an entity such as a corporation or LLC. They could form a Trust (sometimes called a land trust) and hire a Trustee.

The owner will be named on the deed. You, the lender, will get a mortgage where the “owner” of the property has agreed to allow you to record a mortgage on the property. This mortgage is a lien against the property and gives you the right to own the property in case of default by the owner.

The promissory note states the terms of this loan and how you are to be paid back. It should always have the borrower’s personal signature on it along with whoever is on the deed.

In the end, it is simply a matter of saving time and a lot of hassle to simply insist that it be the borrower him or herself who signs the promissory note and/or any contracts.

Item #8: Your Rights in Case of Default

You have a number of rights if your borrower stops paying. Your rights are as follows:

- Accelerate payment on the loan
- Take the property
- Go after the borrower personally

In some states, before you can take possession of the property or go after the borrower personally, you must provide proof that you have made a demand for payment, and that you satisfied the requirements of the state in collecting on a loan.

The importance of hiring an attorney once the borrower has missed a payment must not be overlooked. This will ensure that your foreclosure proceedings are according to state law.

Any fees that may be incurred as a result of the default or late payment must be paid by the borrower in order to reinstate the loan. This must be stated specifically in the promissory note, so that there is no question on the validity of the fees should there be litigation.

Item #9: Repairs

When it comes to repairs that need to be made on the property, it is in your best interest as the lender to be certain that the money allocated for repairs is used for repairs.

Do not let the borrower hold the repair money, trusting that the repairs will get done. It is not a financially sound practice. It is a risky assumption when your money is at stake.

Have the attorney, escrow agent, or Title Company hold the money in escrow and have them prepare an escrow agreement to be signed by the

appropriate parties. The escrow money for the repairs should be released as follows:

- 1st Release – 1/2 of repair funds at the time of closing so the borrower can get started.
- 2nd and Final Release – Remaining repair funds should be released at the point of 50% completion.

Note: If you're ever in doubt as to whether or not the escrow amount is enough to cover repairs, ask the borrower to get an estimate from a contractor and match the items in the estimate to the items on the repair list.

Item #10: Second Mortgages

Make certain that you are not making a second mortgage behind a first mortgage, without having verification that the first mortgage is still current, or will be brought to being current at the closing. There should be no short-term balloons on the first mortgage that could possibly jeopardize your position.

Item #11: Never Make Out a Check Directly to the Borrower

In order to be certain that the funds disbursed at closing go exactly as stated in the settlement statement, you should never make out a check directly to the borrower. Instead follow these steps:

- Your check should be made directly to the closing or escrow agent.
- The closing or escrow agent will disburse funds at closing and hold escrowed funds.
- The lender must not bear any expense.
- Your only expense is getting the check to the closing agent.

Item #12: Assignments of Rents

All closing agents can prepare an “assignment of rents” that may be signed by the borrower with little to no extra cost to the borrower. An “assignment of rents” allows you, rather than the borrower, to collect any applicable rents when due directly in case of default.

Even though the mortgage provides for collecting rent while in foreclosure, it is a good policy to have a separate agreement clarifying the terms.

Item #13: Default Steps

Should your borrower fall behind in his or her payment by 30 days and has not made any arrangement for doing so, turn the account and its situation over to your attorney to take action. This allows you to be certain that the most beneficial and legal actions will be taken for all delinquent accounts.

Any fees that may be incurred will be paid by the borrower to reinstate. It is always better to take action sooner rather than later. You gain nothing by waiting.

The above list is a good foundation for the creation of the right mindset, attitudes, and policies for maximizing your profit potential when lending in a real estate situation.