

# TALES FROM THE TRENCHES™

## BY BARRY C. MCGUIRE

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July, 2015

### AGREEMENTS FOR SALE: DEFINITION AND OPPORTUNITIES

Mortgages are impossible to assume in Canada (even in Alberta) without first qualifying for the mortgage. An Agreement for Sale (AFS) is a seller financing strategy that give you control of a property without a bank! I repeat, without the bank.

#### **The Agreement For Sale Contract**

You can buy a property or sell a property, and here is the correct terminology, 'by way of agreement for sale.' In either case, a real estate purchase contract (often called the 'offer' or 'offer to purchase') is submitted to the other party and the offer clearly says that the transaction is proceeding, 'by way of agreement for sale.' The buyer pays a certain amount of the purchase price by cash and the balance owed to the seller is described as the 'unpaid seller's equity.'

Remember, this agreement does not absolve the seller from making the usual mortgage payments. The buyer makes payments to the seller under the Agreement For Sale. If the seller has an existing mortgage, they must continue to make payments to their lender.

Depending on whether you are a buyer or seller, your AFS document needs to take care of things like assignability, insurance, taxes, upkeep, repairs, items of default, remedies payouts, renewals, interest rates and how they are calculated, responsibility for keeping existing financing up to date and what happens if it isn't, and numerous other details.

**N.B.**, if there is an existing mortgage, you usually want the term of the AFS to match up with the term of the existing mortgage. That way, when your mortgage is due, the AFS is also due. Big bonus: your AFS has a clause that allows for, and leaves you in control of, a renewal of the AFS that is tied to a renewal of the existing mortgage. Try hard for this.

Most law offices do not have a sophisticated version of the Agreement For Sale as it does not come up very much in their practice. We at RMLO Law LLP are more familiar with these documents than most, so for AFS in Alberta, get in touch with us! Otherwise, we ***strongly recommend*** that you stay in control of the drafting of the AFS document. Make it clear if you are the seller, that the seller's lawyer is preparing the Agreement for Sale document at the buyer's expense.

Why is an AFS different? I can hear the wheels turning. "What's the big deal? Isn't this just like an assumption of a mortgage?"

**Here is the key to the magic of the AFS: *Title remains in the seller's name!***

The seller continues to make his mortgage payments to his bank. You pay the seller.

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### Protecting The Buyer

If title isn't in the buyer's name, how does s/he protect her/himself? The buyer or buyer's lawyer has the right (but not the obligation) to register a provincially specific notice against the title at the Land Title(s) Office. The notice claims an interest in the property as a buyer under an Agreement For Sale. However, that buyer will not get title until s/he pays off the seller, usually by arranging new financing. The seller then pays off her/his old mortgage with some of the AFS payout monies and pockets her/his profit. The buyer discharges her/his notice. In our experience, use of the AFS does not trigger an existing mortgage 'due on sale' clause and does not seem to bother any existing lender. Of course, a lender might take a different view and if the lender wants to fight, you don't. Think about your exit strategy in these circumstances.

### Sellers with mortgages often want to sell, but can't do it in the usual way. Why?

Let's look at some examples:

- The seller has little or no equity. They bought at the height of the boom. Prices have fallen. Their high ratio mortgage now has a principal balance larger than the fair market value of the home. They can't sell it with a realtor because real estate fees will take up \$10,000 plus dollars that they don't have. Remember this is negative equity. Even if they do sell, chances are their mortgage is closed and paying it out would trigger a large payout penalty. Think of the negotiating possibilities for you as an investor buyer under this scenario.
- The seller just can't make payments or needs to sell an existing home before buying a new home.
- The seller has positive equity but doesn't need this money. Let's be realistic. Most sellers need the money from their sale, but some don't. You can show the seller how to potentially save thousands of dollars in real estate commission and payout penalties, earn a better return on her/his equity than s/he could in the bank, and, if the seller is also an investor, to defer profit on her/his taxable gain.

Buyer, (*you*), now controls the property. This is powerful! With a properly negotiated and drafted real estate purchase contract and AFS you can:

- assign your interest in the AFS, in other words sell your contract, or;
- lease-option the property to a tenant buyer, or;
- sell an option without a lease, or;
- make a straightforward sale at a profit to another buyer, or;
- keep the property in your Buy & Hold portfolio.

An AFS can work well for the above examples. Plus, sellers usually *love* that title remains in their name.

**No matter the year or economic situation as you read this, it's a great time to find an AFS opportunity.**

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This strategy will give you another chance, another arrow in your quiver to ensure that, regardless of what happens with the economy in the future, you will thrive when others complain that the market is bad and there are “just no deals.”

If you come to one of my workshops or retain me as your lawyer, I can show you how AFS is a proven real estate investment strategy that will allow you to take control of properties for very little money down. Maybe one of the best things about AFS is that it leads to so many exit strategies. You actually don't need a clearly mapped exit strategy right from the start. Yes, the deal has to work for you in a cash flow sense, but you don't need to know your exit the day you get the keys.

Let face it, AFS is not a household concept. Many lawyers don't even know what it is or how to advise on it. You will have to explain to sellers. Does that make AFS impossible? Absolutely not! Personally, I think this obscurity and lack of knowledge is great. Why? That means we have the AFS strategy to ourselves.

Remember, whatever strategy we use, make sure it's win-win! No taking advantage. If a seller can achieve their objective without an AFS, tell them. Don't tie up their home when you could point them in another direction. However, if your analysis tells you that an AFS will get them what they need, then full speed ahead!

### Agreements For Sale Lovely Concept... But, Are There Any Real Deals?

Our Rapid Cash Program students tell the story in their own words.

**Property Type: single family home / Purchase Price: \$340,000 / Money Down: \$1,600**

Seller Financing: \$338,400

Seller's Issue / Problem: seller wanted to build new house and was having trouble selling due to condition of the house

Potential Profit / Exit Strategy: 2.5 year Rent-to-Own client who purchased the property for \$365,000. (this was one of my first deals and I did not get the benefit of mortgage principal pay down - if I had, I would have made another \$10,000 or so.... Monthly payments were high, so cash flow was breakeven)

**Profit after expenses: \$22,500**

**Property Type: townhouse / Purchase Price: \$228,000 / Money Down: \$3,210.00**

Seller Financing: \$224,857 bank mortgage

Seller's Issue / Problem: could not afford payments

Potential Profit / Exit Strategy: Found a tenant who purchased the property in 6 months time for \$245,000.

**Profit after expenses: \$14,675.00**

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**Property Type: townhouse / Purchase Price: \$185,000 / Money Down: \$5,000 (to pay mortgage & tax arrears)**

Seller Financing: Bank mortgage \$180,000      Sellers were divorcing, no equity.

I moved in, did paint and carpet, sold one year later for \$250,000.

**Profit after expenses: \$55,000**

**Property Type: Single family starter home / Purchase Price: \$275,000 / Money Down: \$7,500**

Seller financing: Mortgage. (About \$20k in unpaid equity).

Seller was cash-strapped and got second mortgage to alleviate financial stress, obviously not considering she would not be able to make the payment on the second. Plus house was half-renovated (and not very well), and the market for "project houses" is quite small. We flipped this one. Sold 4 months later for \$362,000 (a new record high for the neighbourhood). Could have easily refinanced (to pay for renovations) and then done RTO. Would have been more profitable.

**Profit: \$87,000**

**Property Type: 2 fourplexes      Purchase Price: \$780,000      Money Down: \$0**

Seller Financing: Bank mortgage      Sellers were divorcing, not good managers.

**Exit Strategy: Long term hold – 8 doors... for NO money down!**

**Property Type: Single family home / Purchase Price: \$445,000 / Money Down: \$1,000**

Seller Financing: remainder seller financed (about \$75,000 in unpaid equity, the rest mortgage) Payments would cover mortgages. No unpaid equity payout till maturity.

Seller hated being a landlord. He had a string of bad tenants and got tired of huge repair bills. We later learned he also used high-interest debt to pay the repair bills. Seller requested for us to cash him out early so he could eliminate debt. In exchange, price was lowered to \$410,000. Property is rented for \$2600 per month. Will likely do RTO after this tenant leaves. Property appraised at \$485,000

**Predicted Profit: \$75,000 + cash flow**

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**Property Type: Single family (2 storey) / Purchase Price: \$270,000 / Money Down: \$50,000**

Seller Financing: \$220,000

Seller's Issue / Problem: need to move immediately- unable to sell traditional method because daughter and her family also live there, not easy to show house or stage it for proper sale

Potential Profit / Exit Strategy: House valued at \$320,000 at time of purchase....used as my primary residence initially and then one year later I turned into a Rent-to-Own..... renter will purchase home Oct 30/15 for \$396,000. The total profit from this home will be \$126,000 plus monthly cash flow of \$500 per month x 36 months = \$18,000....

**Predicted Profit: \$144,000 over a 4-year period.**

**Property Type: Single family (w/legal suite) / Purchase Price: \$260,000 / Money Down: \$10,000**

\*\* This was a referral from the client in example #1 \*\*

Seller Financing: \$250,000

Seller's Issue / Problem: Seniors wanted to move into retirement home...did not want the hassle of traditional sale and saw how easy things went with a relative in the above example.

Potential Profit / Exit Strategy: Since I only had financing for 9 weeks while I did some updates and repairs, I chose to sell the house.... (if it could not sell I did have financing arranged) initially I was told the value of the house would be \$325,000 with small repairs ....but in the end had multiple offers and sold it for \$369,000. Total profit was \$109,000 - (down payment of \$50,000, realtor fee of \$20,000 and repairs and legal costs of approx. \$9000) ..... I owned the property for a total of 6 weeks.

**Total profit of approximately \$30,000**

**Property Type: Single family home / Purchase Price: \$109,000 / Money Down: \$0**

Seller Financing: \$109,000 (bank mortgage)

Seller's Issue / Problem: Empty house.... Huge problems with plumbing (tree roots) and needed many house repairs and updating.

Potential Profit / Exit Strategy: Initially I was going to do the repairs and either do RTO, sell or a regular rental (I had 3 years for mortgage payout on the AFS) But in the end, because this property is one hour away, and many complicated repairs needed... I choose to do an assignment of the contract to a contractor. With repairs (\$25-30K) to this house, the new value would be at \$180- \$200 K. I sold the assignment for \$10,000, still leaving the contractor plenty of room for a nice profit once repairs completed.

**Profit \$10,000**

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### Lessons Learned:

1. AFS is a legitimate, time tested strategy
2. AFS is not well known, we basically have it to ourselves
3. My students and clients are finding deals and making a ton of money.

**WE HELP PEOPLE BUY & SELL REAL ESTATE IN ALBERTA**  
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