**\*\*\* PRIVATE MONEY TUTORIAL: PRIVATE MONEY DEAL STRUCTURING**

[**http://rehabvaluator.com/content/private-money-explained/?inf\_contact\_key=cf8c3ce30d1ff74634f9e56d3bbe4f032b11d68eaddea358e443f91f4f846dad**](http://rehabvaluator.com/content/private-money-explained/?inf_contact_key=cf8c3ce30d1ff74634f9e56d3bbe4f032b11d68eaddea358e443f91f4f846dad)

**Private Money Lending Explained Once and For All!**

**PRIVATE MONEY.  EXPLAINED. ONCE AND FOR ALL.**

I wanted to write a blog post about a very important topic that I often get questions on:  private money.  I wanted to clear up some misconceptions and hopefully add some serious value to your day with some facts, some brutal honesty, and some information that is sorely lacking in clarity out there.  I also touch on some concepts you may not be familiar with when it comes to financing, like “credit partners”, “joint venture partners”, and a few others.

It took me some time to put this together so please read carefully, leave your comments, questions and feedback at the bottom.

Also, if you find this valuable, please share on Facebook and Twitter using the buttons below.

**Private Money – The “Dreaded Question”**

I get about 5 emails a day saying:

*“Daniil, can you send some private lenders my way?  I have a great deal!”.*

And the answer is a flat out *“No”.*

It’s not because I am a bad guy or don’t want to help you.   But rather because **you don’t have a fundamental understanding of what a real private money lender looks like.**

So let’s backtrack a bit and go over some basics, then tackle your misconceptions and then finally give you some ideas on how to find legitimate private money:

**“Private Money”** –  this term is widely misunderstood, at least partly because of faulty advertising online.  The term “private money” refers to loans made between individuals.  When you get a “private money” loan, it’s typically from a friend, a business contact, an individual you’ve built a relationship with.  Unfortunately lots of hard money lenders advertise themselves online as “private money” which causes a whole lot of confusion.

Don’t believe me?

Google “private money lender Denver” or “private money lender Richmond” or any city for that matter.  You’ll find nothing but hard money lenders advertising their services.  I’ll explain the difference below if you don’t understand it – it’s HUGE.

**Difference between Bank Vs. Hard Money vs. Private Money Explained:**

So….let’s back track even further  and break down the types of financing available out there for real estate deals briefly so you understand the difference.

1)    **Bank Financing.**

When it comes to investor loans, these can be broken down into 2 categories:

**Conventional Lenders.**  This is the 30-year mortgages that Wells Fargo, Chase and other big banks provide mostly on owner-occupied properties.   They do, also, provide loans on investment properties.  [But to qualify is extremely difficult](https://www.fanniemae.com/content/eligibility_information/eligibility-matrix.pdf) and there is a strict limit on how many financed properties you can have before they cut you off.

* The conventional loans must all fit neatly into a strict set of guidelines set by Fannie Mae or Fredie Mac to be underwritten because after origination, they all get sold into the secondary market by the banks that originated them.

**Bottom line:**  if you want to finance investment properties, whether it’s flips or buy/hold, forget about going this route.  Flips are out of the question period – they won’t finance rehabs unless it’s your personal residence.  And for buy/hold, it’s painful and you probably won’t qualify anyway.   I would rather get a massage from Edward Scissorhands than ever go through that underwriting process ever again.

**Local Community Banks and Credit Unions.**   Unlike Conventional Lenders, these are small, local banks who typically do NOT sell the mortgages they originate.  Instead, they keep them “in-house” or in their portfolio, which is why they’re called “portfolio lenders”.

Because of that fact, most of these banks can set their own lending guidelines and lots of them are better pre-disposed to working with investors.

Pros:

* They will finance rehab projects (including flips and new construction).   I am currently financing a number of new construction projects where the bank is funding 85% of the total cost of my project .  \**Every bank is different and has different appetite for certain types of loans.  So you may talk to a few before you find the right one*
* They will finance investment properties for buy/hold with no limits on how many you can have.  There is no silly “10 maximum property” limit, though each bank will have a maximum desired “loan concentration” for a given investor.  (That limit is typically well into the millions though. )
* Local community banks are MUCH easier to deal with than conventional lenders.  The hierarchy and bureaucracy when it comes to underwriting is much easier to navigate.  They understand the local market, they understand our business and they are MANDATED to lend locally

  Cons:

* You will still need “skin in the game”.  For example if you’re financing a flip, you’ll still need 15% cash in the deal if they finance 85% of your total cost.
* You will still need to meet underwriting standards of the particular bank:  FICO score, debt to income, etc.  They will look at your global balance sheet, cash flow, and still require “personal recourse” for your loans
* Most of their loans are basically “commercial loans” even though they may be on residential properties.  That means these will NOT be 30-year fixed rate mortgages.   The local banks are too smart for that.  Most of the loans I’ve taken out locally have had a 20-year amortization with a 5-year call or reset.   This creates some serious interest-rate risk for you as a borrower 5-years out (or whenever that reset or call occurs).

**Bottom line:**  If you are going to seek bank financing for your real estate deals, “portfolio lenders” are the way to go.  You’ll deal with smart loan officers who “get the joke”, not some idiots 6 states away. But you’ll still need to qualify and 99% of the time you’ll need to bring some kind of cash or equity to the deal, whether it’s for flips or buy/hold.

**An idea:**If you want to go after bank financing and can’t qualify for loans yourself,  find what’s called a “credit partner”.  A credit partner is someone who looks very good on paper:  great, verifiable income, great credit score, low debt to income ratio.  They will co-sign the mortgages with you in return for a piece of the deal.  Assuming they bring no cash (just their credit) to the table, it can be a great deal for someone to become a passive investor in your deals solely through taking on some “mortgage risk”.

2)    **Hard Money Lenders.**

These are the guys that will eat your lunch and then bill you for it.  They often advertise themselves online as “private lenders” which just serves to confuse the crap out of unsuspecting investors.  Now, look, there ARE positives about dealing with the hard money guys so let’s talk objectively here for a second.

If you are looking to buy and hold, then hard money is NOT an option for long-term financing.

But if you are doing flips, then hard money lenders play a legitimate role in the marketplace for this types of deals.

Pros:

* Typically very easy to qualify – they don’t care about your credit, balance sheet, FICO,  income, etc
* Fast money – can typically close quickly (faster than bank financing)

Cons:

* VERY expensive money, so you need to make sure your deal has enough profit margin to handle the “cost of money”.  You’ll typically be charged anywhere between 3 and 6 “points” or % of the total loan, PLUS 10-16% interest rate on top of that.   If you look hard enough you’ll find even more expensive loans out there.  For a typical flip that takes 6 months, on average your cost of money will end up being 10-15% of your project cost (or loan amount).   That takes a lot of “meat off the bone” if you know what I mean.
* Short-term money.   Hard money lenders make their profit on “turning their money” and thus on points.  They want to lend, charge the points, get that money back quickly and then put it out there to another investor, charging points again. So most hard money loans will typically be for 6-12 months, after which the loan is due.  Terms will vary, from giving a hard money lender ability to take the property after the loan is due (or at least start foreclosure) to simply bumping up the already high interest rate to a sky-high “penalty rate”.
* These days, even hard money lenders will want to see “skin in the game”.  In other words they’ll want to have you bring some cash to the deal.

**Bottom Line:** very expensive, very short-term money and 100% financing is going to be very tough if not impossible to get there, just like with bank loans.  Make sure you have an assured exit strategy if you take on hard money.

3)    **Private Money Lenders.**

Ok, we finally get to the topic with which we started!   Private money.  The REAL private money.   Once you are able to find TRUE private money, the advantages are immense vs. banks or hard money lenders:

1. 100% financing for your deals
2. Long-term money with no calls or resets
3. Flexible underwriting (no credit checks, etc)
4. Cheap money (especially vs. hard money)
5. Scalability (no max loan or property limits like with conventional financing)
6. Non-recourse financing (liability limited to the property or company, not your own personal assets)
7. Etc

**So how do you find private money?  Let’s start with definitions:**

**A Private Money Lender:   This is an individual with whom you have a relationship of trust who chooses to invest in your deals.  It is NOT a professional lender, a hard money lender, a money broker, a transactional funder, or anything of the sort.**

A typical private money lender is a guy you work with at the office, your dentist, your doctor, the guy/gal you work out with at the gym, a retired aunt or uncle, your accountant, someone you used to do business with, a guy you met at your church, a friend of a friend who is looking to diversify, etc.  Whoever they are, they are someone who has been relatively successful in another profession and now has some idle cash or a 401K/SDIRA which is not earning them much.  They are unsatisfied with their returns they are currently getting.  Maybe they even thought about real estate already but don’t have the time/knowledge to start investing themselves.

Whoever they are, they are someone with whom you have built or are building a relationship.  You’ve talked to them about your real estate deals a few times or maybe just about your strategy.  They’ve told you about their “money problems” and you realized that you can help them by letting them invest with you.

Do you see where I am going with this??

A real private money lender is not someone you’ll find online by googling “private money lender”.  And they are certainly not someone who I can refer to you.  So please don’t email me asking me if I can “send some private money lenders your way”.  MY private money lenders know ME, trust ME, and are typically local to MY market.  I’ve spent a long time building that trust, credibility and track record with them.   Even if I wanted to send them your way, which I most certainly do NOT, they would have a hard time working with someone who is far away and whom they don’t know at all.  Relationships take time to build.   But once you build them, the pay off is amazing.

I promised you some harsh honesty and here it was.

**==>So how do you find, build, create, mold your own private money lenders?  <==**

I break that down into 3 categories:

1)    Tap your existing network

2)    Expand your existing network

3)    Market for money

1)    **Tap Your Existing Network:**    Sit down and make a list of all of your friends, relatives, colleagues, people you go to church/synagogues with, people you work out, your doctors, dentists, CPA, your cash buyers, your banker, your title co people, etc etc.  Write it down and make a list.

Now, you don’t need to go asking these people for money.

Asking anyone anytime for money is a HUGE mistake.

Read that again.  Did you read it?  Write it down if you need to.  Don’t ever ask anyone for money.

**Instead, reframe your mindset:**

**Change of frame 1:**  You are not looking for money.  You are a capable, knowledgeable, driven real estate investor and deal maker.  From time to time, you have opportunities for other individuals to work with you, invest along-side you, and earn a great passive return secured by real estate.

**Change of frame 2:**  You may have money problems because you are poor or broke or just struggling to make ends meet.  BUT…the middle class, the wealthy, even the ultra-wealthy have money problems too.   They have worked hard to become successful in their respective fields, save up some money, maybe accumulated good size 401-Ks but now they don’t have a decent place to invest their money.  They are worried about preservation of capital (stock market doesn’t guarantee that at all).  They want cashflow (very few stocks have a dividend yield above 3%).  The CDs these days pay less than 1%.  You get the picture?

So you are the SOLUTION to their problems.  Not someone begging for their money.  You are the competent, ethical, determined, driven, practical solution to their “money problems”.

So…once you reframed your mindset, you can now start talking to people in your network about your business and your goals the right way.

**Say this:**  *“Hey, I am starting to do some really exciting deals here and from time to time I’ll have an opportunity for people to invest totally passively in my deals and earn great returns.  Do you know anyone that would be interested in briefly discussing this?”*

Get it?  You don’t even have to ask the person you’re talking to directly – just ask them if they know someone.  If they themselves are interested in discussing your deals, they’ll tell you.

Some things that may help you:

* A simple credibility kit
* A sample deal profile that shows how the deal will work and potential returns to your investors ([like this](http://rehabvaluator.com/3710WestcliffeAveFlipMarketingPresentationforPrivateLender.pdf)) ([or like this](http://rehabvaluator.com/3710WestcliffeAveFlipMarketingSheetforPrivateLender.pdf))
* Put together a simple chart that shows current CD rates, historical stock market performance indicators, etc – to show people that your projected returns are higher than alternative investments AND secured by real estate

**2: EXPAND Your Existing Network:**   If you sit down and make a list as I suggested above and then exhaust that list, or maybe that list is fairly small, then go and expand your network.

          YOUR NETWORK = YOUR NET WORTH

So you want to not just blindly expand this network, but you want to expand it with the right kind of people.  You want the right people in your network.

Some ideas:

* Volunteer at a local charity.  People that have achieved a certain level of wealth and comfort often like to give back.  Local charities are great places to meet quality people. You don’t have to give money – just your time.  Finding a common passion for helping others is a great way to connect with someone and build a relationship of trust.
* Local Toastmasters Club.  Every town has a bunch of them.  This is where entrepreneurs, business professionals, and executives go to hone their public speaking skills.
* Your church/synagogue/etc.  They all have social functions.  Go meet people.  Get to know them.  Talk about what you do – but from a “power” position, not a “needy” position.
* Local Chamber of Commerce.  You’ll find all sorts of events hosted by your local chamber in your town.  Great networking opportunities.
* Local Real Estate Investment Clubs – you will every once in a while find people who attend because they are curious about real estate investing.  They have often thought about investing, maybe they even dabbled.  But they don’t know what the hell they’re doing and often don’t really have the time to do it properly anyway.  They can be great potential partners.

**3: Market For Money:**

This is not something I’ve ever done or choose to do, but there are plenty of people that do this and plenty of gurus that teach it.

You can create direct mail pieces and target:

1)    Lists of accredited investors in your area (pulled from sites like [www.listsource.com](http://www.listsource.com/)or [www.melissadata.com](http://melissadata.com/))

2)    Lists of people doing actual private money lending in your area currently.  This data can be pulled from your local courthouse county records, or again, from[www.listsource.com](http://www.listsource.com/)

3)    Lists of people with self-directed IRAs

4)    Etc

Now, if you choose to go this route, I highly suggest you get yourself familiarized with the current SEC rules and regulations.  They are not someone you want to mess with.  Do your research and maybe consult a competent SEC attorney about what you can and can’t do when it comes to marketing for money.

Here’s the basic rule of thumb though:  until you have an existing relationship with a potential lender/partner (you’ve had a few face to face meetings or calls), do NOT discuss any deal particulars, particular rates of return, etc.

Do NOT do this:  mail someone a letter saying “I have a great deal with a guaranteed 12% return on your money!!”.

Do THIS instead:  mail someone a letter saying “My name is \_\_\_\_,  and I currently have a successful real estate business \_\_\_\_.  From time to time I have opportunities for others to invest passively with me and earn great returns secured by real estate.  If you’d like to discuss this further, please call/email/visit my site/etc”.   Be VAGUE when you first contact people.

In your letters provide as many ways to contact you as possible.  It also doesn’t hurt to have some sort of a “bribe” for them to reach out to you, like a free report that helps them someway.

\*\*\* IMPORTANT:  Please consult with a qualified SEC attorney to make sure your marketing materials and mailing pieces do not break any of the SEC rules that have to do with soliciting investments.  The rules keep changing and it’s important you stay on top of them, protect yourself and your investors!

**Some Advanced Concepts and Resources for You:**

Now you should understand what real private money is and hopefully have some good ideas on how to find it.  The beauty of private money is that it’s totally flexible in terms of how underwriting and deal structuring is performed.   Whatever you and your private money lender agree on, goes!

So be creative in how you structure deals to meet the needs of your lenders/partners.  You can:

* Offer just a fixed % interest rate
* Offer points and a fixed % interest rate
* Offer points only
* Offer a fixed % interest rate and a profit split on your deals
* Offer just a profit split – this is called forming a “joint venture”
* Etc etc

Obviously, as a real estate investor, your #1 objective is to lower your “cost of money”.  You want your funding to be as cheap as possible.  But you also want to make it attractive for lenders to work with you.  Sometimes that means offering them a “carrot” in the form of a high potential return if the deal works out the way it’s supposed to.

[Watch this video if you want to learn a few various ways to structure private money deals](http://rehabvaluator.com/case-studies/private-money-structuring)

We also relaunched [Bank Elimination Blueprint](http://rehabvaluator.com/webinar) recently which teaches joint ventures, private money raising, etc.  This is DEFINITELY worth checking out!

And, of course, if you are NOT using [Rehab Valuator Premium](http://rehabvaluator.com/upgrade) to create deal pitches and present your deals to private money lenders and hard money lenders, then you really should…asap.

Leave me your questions, comments, feedback below and share this with your friends/colleagues if you found it useful.

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