1 Understanding Tax Liens and Deeds

Nothing is certain but death and taxes.

—Benjamin Franklin

Benjamin Franklin first uttered those words in 1789, and I'm not sure that much has changed since then. Of course, the concept of taxes goes back much further than that, as recorded history shows that taxes have been collected from people by governments, monarchs, and kingdoms for thousands of years.

But what happens when people don't pay their taxes? Some go to jail, some may lose their property, or centuries ago they may have even been hanged. Nothing that drastic takes place in today's society, but taxes are still an important part of life, and they are vital for governments to provide services to their citizens. And with estate and probate taxes in effect, they continue even after your death.

But what does that mean for you? More importantly, how can the tax system actually provide a road to wealth for you and your family? That's what *Zero Risk Real Estate* is all about. For more than 30 years, I have been actively participating and investing in real estate, both personally and with clients and students from all over the world. While there are many ways to make money in real estate, nothing comes close to the long-term growth, stability, dependability, and relative safety of tax lien investing.

Another benefit of tax lien investing is that it does not take a large amount of money to get started. You can buy tax liens with anywhere from a few hundred to a few thousand dollars if you like. Obviously the more you invest, the more you will get back, but unlike buying homes the traditional way, it does not cost hundreds of thousands of dollars to get into the game.

I will not only show you how it's done, I will prove it to you through specific real-life examples of deals that my students and I have done. I'll give you the forms, letters, checklists, and exact methods that I have used to get deals closed. And at the end of the book, I'll give you a website where you can actually go and watch instructional videos of me doing actual real estate investment deals.

But *you* have to make the commitment to do it, and along the road many people will throw obstacles in your path. You see, we all know that family, friends, and associates may mean well when they try to give you advice. Saying things they think are going to protect you, they may tell you that tax lien and deed investing is a scam, too good to be true, or even illegal—*none of which is true*.

I call them *Gremlins*—well-meaning people who think they know what they're talking about, but really just end by mucking up the works. There are a variety of reasons why these Gremlins are trying to spook you away from something that is financially lucrative and which produces a high rate of return for you. Their good intentions are obviously to try to protect you from yourself. They probably just don't understand the entire tax foreclosure process, or there is also the possibility that they may simply be afraid of what will happen if you succeed. It is unfortunately true that people like to see other people fail. Why? To feel better about themselves. You see, since they are doing nothing to improve their lives, they want to encourage everyone else to do nothing. This way they can justify their behavior. If they see you going out and working hard and taking action, then they feel guilty for not doing the same thing for themselves. It's much easier to sit back and say "that will never work" than it is to go out and try to make it work.

In order to succeed in your real estate investment business, the first lesson I want to share with you is to stay away from the Gremlins. They will try to prevent you from moving forward and becoming successful. The best way to handle the Gremlins is to ask them if they have ever personally tried tax lien or tax deed investing. Most likely they have not.

Making changes in your life is a positive thing. If you feel you are stuck in a hole, you need to dig yourself out by shifting your thought process from "what if I can't get out" to "what is the fastest and best way to get myself out." Making the decision to get out of the hole, developing a course of action, and setting a goal to try something new is just the beginning. If you want to truly succeed, then you have to be willing to do the things that others are unwilling to do, like investing in tax liens and deeds.

Change takes developing the right attitude and being able to withstand negative influences. Change is what it takes to become successful in your endeavors no matter what you choose to do in life. Make a commitment and follow through. You won't be sorry. Don't worry—your friends and family will come around soon enough begging you to tell them how you did it, and pleading with you to share it with them.

Real Estate and the Property Tax Process

As I mentioned, real estate and property taxes have been around since the beginning of time, and kings, countries, and governments have been collecting taxes for many different reasons since the dawn of man. Taxes are very much a part of everyday life. In the United States, similar to other parts of the world, owners of real property are required to pay taxes to their local government. The local government in turn uses these taxes to provide its residents with critical public services such as schools, roads, hospitals, transportation, libraries, and fire and police protection. Without these taxes being collected, public services would eventually cease, and mass chaos would ensue.

In more than 3,200 county and local jurisdictions throughout the United States, there are billions of dollars in overdue and unpaid property taxes. In just one county alone in Indiana that I was reviewing the other day, there is more than $55 million worth of overdue property taxes that are delinquent right now.

There are dozens of reasons why people don't (or can't) pay their property taxes. Divorce, death, financial problems, job loss, estate or probate issues, emotional distress, or foreclosure, to name just a few. However, if a property owner fails to pay taxes for any reason, the property is then deemed *tax delinquent*, and the government must take the necessary steps to bring the property back into compliance with the law.

These unpaid taxes take away money from municipalities—money they desperately need to use for community services. To be fair, local governments do not blindside property owners with sudden and unexpected action in order to collect past due taxes. They offer every reasonable opportunity, in terms of both time and payment options, for owners to make good and pay their tax bill. Property owners certainly know what their tax amounts are, and they are given advance notice of payment due dates in order to plan ahead. In most cases, when a property owner has mortgaged the property, the lender also established an escrow account to collect amounts to pay future taxes to make sure that the money is there when needed.

However, if the tax payments don't get made, there comes a legally mandated point when the government is left with no recourse, other than to try to recoup the taxes in other ways so that its public services and other citizens are not negatively affected by the reduction in tax revenue. So what are these other ways by which the government can recover taxes left unpaid by a property owner? While there are differences in how different states and counties recover these taxes, about half the states use what is called a *tax lien* system, and the other half use a *tax deed* approach. Both options give local governments a legal interest in the tax delinquent property, and allow them to do whatever needs to be done to get the taxes on that property flowing back into the public coffers.

Obviously, this is an unfortunate scenario for the property owner as well as the local government. Both are now saddled with financial burdens they cannot meet on their own. The property owner has a property that has become unaffordable, and the government has a property it certainly does not want to own, although they have a legal obligation to collect the taxes they direly need.

So to minimize the stresses to both parties, they seek relief from an outside source, a third party who can bridge the gap between the property owner and the government. This is where you come in. You are seen as the knight in shining armor and the savior of county tax revenues.

By you investing in tax liens or tax deeds, you are enabling the county to collect the taxes so that they can provide their residents with city services that they need and expect. In return, you benefit by receiving a legally mandated high rate of return (interest) on your investment, which is secured by the property and the taxing authority of the government. Since the county controls the tax lien or tax deed sale process, your investment is safe, secure, and legal. This is the basis for *Zero Risk* investing.

WHAT IS A TAX LIEN?

Investing in real estate is one of the most profitable markets available today. It allows you to make money multiple times from one simple investment and can help you increase your net worth, cash flow, and financial freedom by putting more of your hard-earned money in the bank. If you are working toward finding new ways to earn and invest, then looking at real estate is a good way to go. And if you are just starting out in this business and don't know where to begin, then tax liens are the perfect vehicle to get your feet wet and start to learn how to make money in real estate.

Whatever type of property you may invest in, whether it is residential, commercial, or industrial, there are several taxes that are attached to the property that can make you money. Taxes can make you money? Yes! But only when you take the place of the government and the taxes are then owed to you! Taxes are levied in a variety of places with the purchase of a property or home, and when they are not paid by the owners, they become tax liens. Tax rates are determined by the state and county where you live, based upon the price of housing in your neighborhood and assessment rates.

Tax liens begin when someone doesn't pay their taxes on a property that they own. If the taxes become overdue, the county has the right to sell the tax interest (or lien) to someone else. Usually, people who owe the government taxes will be given a certain amount of time to pay them. If they don't get paid after that time, the tax lien turns into a certificate that can be bought by an investor. Whoever purchases this document will then be given certain rights over the property, and those rights can change after a given amount of time has elapsed.

First, let's go over the meaning and differences of *tax liens* and *tax deeds*, and explain how you as the outside investor can benefit financially while you help local governments get back to providing much-needed services.

> In the simplest of terms, a *tax lien* is an interest in the property that gives whoever owns that interest certain rights to the property—*but not ownership.*

When a tax lien is placed against a piece of real estate, it means that the owner cannot sell, mortgage, transfer, or refinance it until the lien is paid in full. They cannot do anything that will affect the title of the property. Anyone who does a title search on the property will see the lien and not want anything to do with the property until that lien is satisfied. Of course there are penalties and interest that have to be paid as well on the tax lien, and that's where your opportunity comes in.

When you invest in a tax lien certificate, you are basically waiting for the owners to pay off the back taxes they owe, including the interest and penalties. Now before you get nervous, let me assure you that you do not have to play collection agent and actually go out and collect the taxes. The government has a built-in system to take care of all of the dirty work for you.

The county tax assessor, or treasurer, will still collect the past due taxes on the property. But you've been kind enough (or smart enough) to purchase the lien from them at a tax sale, and now you own the county's interest (called the *tax certificate*). The municipality that ends up collecting the tax payment will wind up sending you a check—complete with interest. So essentially what is happening is you are paying the taxes on that property for the person who owes them. Now instead of that person owing the county, they owe you. It's as if you gave them a loan to pay off their taxes.

Now we all know what it's like to loan money to someone and try to collect it. You end up chasing after them for what seems like forever and in the end you end up feeling like the bad guy for demanding to get paid your own money back! Well, think of the county as your own personal collection company. They do all of the hard work and they don't mind being made to look like the bad guy. They will use every method allowed under the law to get your money back to you, *plus* all of the interest and penalties that you are now owed. Sounds great, right? I'm sure your next question is "But how long do I have to wait to get my money"?

The payoff must occur within the statutory *redemption period* that is specified in the law. The redemption period varies by state, and could be as short as a few months, or it could last for several years. Your return on your investment is predictable, however, because interest rates on tax lien certificates are fixed by the local statutes and laws of the state where you purchase them. So while you may be waiting a long time to get your return on your investment, the return is guaranteed by the government and the rate of interest is much higher than you can get from other types of investing.

Rates vary from state to state, but average rates of return can be anywhere from 10 to 24 percent and can go as high as 50 percent annually. States with longer redemption periods generally pay higher interest rates on the certificates, as an enticement for investors. You are certain to receive a nice rate of return because you are investing with the government, and their record for eventually collecting is pretty high. So what if the property owner still doesn't pay? So that you can get a better idea of what happens, let's take a look at a recent example.

> I went to a tax lien auction, and after doing my research I found several liens that were on properties that I felt would be good investments—meaning the properties were very marketable and worth much more than the cost of the liens. I purchased a tax lien for $5,100. The lien was already 12 months overdue and I knew in this jurisdiction that if taxes were not paid within 24 months, then they would go to auction. This meant that the worst-case scenario I was looking at was waiting as long as twelve months to get a return on my investment.
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> The interest rate I was able to get on this lien was 23 percent. I was given the tax lien certificate by the county, and my company's name that I used to purchase the lien was put in public records as the owner of this tax lien. Now all I had to do was wait and see what happened.
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> I received a phone call from a title company about eight months later asking me for a payoff amount for my lien. Apparently the owners went into default and negotiated a short sale with their lender to sell the property. However, because I held the tax lien, the property could not be sold or transferred until I was paid off in full. I did some simple math and conferred with the county to come up with the amount I was owed. It broke down as follows:

Cost of the lien	$5,100
Eight months interest at 23 percent	$782
Penalties for delinquent payment	$288
Total amount owed to me	$6,170

So in just eight months my $5,100 investment made me more than $1,100 in profit!

Just to be perfectly clear, a tax certificate sale is not a sale of land, but rather is a sale of a lien against the subject property. Delinquent taxes are advertised in local newspapers prior to the tax certificate sale, the sale is open to the public, and participants purchase the certificates as investments. The tax certificate sale itself is conducted in a manner similar to an auction. The bidders are essentially extending a loan at a specific interest rate in order to pay the delinquent taxes for the property owners.

All you really need to know is a general understanding of the tax lien certificate investing laws in the state where you purchase them. Tax lien certificates can be purchased through auctions or over-the-counter (what is also known as *OTC*) by anyone, anywhere in the world.

When planned properly, your investment is safe and free of risk as opposed to investing in the stock market or other types of investment methods. Another nice feature is that tax liens are also not affected by the fluctuation of the retail real estate markets. There's always a built-in profit if you follow the process and do your homework.

Tax lien certificate information is also readily available when you know who to contact and what to ask for, and many lists are available directly online. The trick is knowing which ones to buy and when to buy them in order to make them zero risk.

The absolute worst thing that can happen when the owner does not pay the taxes is that they end up losing ownership of the property to the government. Of course, since you now own the tax lien interest instead of the government, you can now foreclose on a property that you purchased for pennies on the dollar *and actually own it outright, free and clear!*

Yes, you read that right. A tax lien is superior in title to any other lien on the property, and this includes mortgage loans. What that means is that the tax lien is in "first" position on title to get paid. If you foreclose on a tax lien, then all of the other liens on the property that are below you (first mortgage, second mortgage, utility lien, and so on) all get wiped out. You now own this property with absolutely no debt on it.

WHAT IS A TAX DEED?

A tax deed, on the other hand, means that the county has already taken actions beyond the tax lien stage. The taxing authority filed the tax lien some time ago, and has already legally foreclosed upon and taken tax possession of the property, and is now ready to transfer ownership of the property to you. This also means that you are buying the property for a substantial discount with an already built-in equity. But remember, there's a reason why someone decided not to pay the taxes, and your job is to figure out why. Some of these properties may be easements, landlocked properties (meaning they have no access to common roads), alleyways, or other types of property that have little or no value.

The best tax deed investments are properties that are purchased for at least 30 to 50 percent below the fair market value of the property. This way, you receive the highest rate of return on the investment and help eliminate potential risk.

Like tax lien certificates, tax deeds are also offered through public auctions or over-the-counter. The rules and guidelines for bidding on tax deeds can usually be found on the county's website or by contacting them by phone or in person. So that you get an idea of how a tax deed works, here's a transaction I completed earlier this year.

> I purchased a tax deed at a county auction for $15,000. This included all of the principal, interest, and penalties the county was owed on the property, plus slightly more since I had to outbid another investor. I had already researched this property and found that by using some simple comparative market analysis (meaning looking at what similar properties were selling for in this neighborhood), this property was worth anywhere from $90,000 to $100,000 if it was fixed up. Before going to the auction I did a drive-by of the property, looked in the windows, and did a thumbnail estimate of what I thought the worst-case cost scenario would be to clean it up and get it ready to sell. I came up with a safe number of $10,000. I purchased the property and was given a quitclaim deed by the county. (Some jurisdictions will issue a Certificate of Title or a Sheriff's Deed, and they are all basically the same thing.) I started my repairs on the property and hired a Realtor to market and sell it for me. She found a buyer willing to pay $95,000 for the property.

So here is how my costs broke down:

Buying the tax deed	$15,000
Repairs to the property	$8,800
Commission to Realtors	$5,700
Closing costs	$3,150
Total expenses	$32,650
Sales price	$95,000
minus:	
Total expenses	$32,650
Net profit	$62,350

As you can see, there can be a great deal of money made in these types of transactions, as long as you know what you are looking for, and if you conduct the proper research in advance. By the end of this book, you'll know exactly how to structure your own deal and cash in for a nice profit.

So to summarize, buying a tax lien certificate is buying the actual debt owed on the property. You now are owed the taxes and take the place of the county. You have the right to collect this money, and if you are not paid, then you have the right to foreclose on the property and take title.

Buying a tax deed means the county has already finished the collection process. They have foreclosed on the property and the county typically owns it free and clear. Now the county is the one selling the property and you can buy it from them. Yes, the county will sometimes make a profit selling it to you, but if you invest smartly, then you will still make a significant profit when you resell it as I did in the above example.

UNDERSTANDING REDEMPTION PERIODS

Of course no one wants to take away someone's property, not the government and certainly not you. As I mentioned previously, owners are given every opportunity to pay their past due taxes and to avoid everything we've just talked about. They are permitted to make payment anytime prior to the tax lien being filed, after a tax certificate is sold, and sometimes even after a tax deed is sold. These are called *redemption periods*.

Once a certificate is sold, the owner can still redeem the property for a certain period of time by paying the back taxes, penalties, and interest to the treasurer or tax collector. These redemption periods can last up to several years in some states.

> During a redemption period you cannot enter, access, or use the property.

It is important to note that during the redemption period, the owner *still owns the property* and has all the rights and benefits of ownership. He or she can still occupy it, rent it out, or even sell it. Of course if they do sell it, then the taxes are paid at the time of sale, and you receive your check. This is because your tax lien on the property becomes a matter of public record, and any title company that performs a closing or transfer of title on the property will have to make sure you are paid off in full before the transaction can close.

As a tax lien certificate holder, your rights are quite limited. You cannot possess or use the property, trespass, or alter the use of the property. This is actually a good thing, since you're just looking for a solid guaranteed investment, not to become a landlord. Your interest in the property is simply a *paper* interest.

In a tax deed situation, it is entirely different in most cases. Once a tax deed has been issued, you now own the property and have to take steps to protect your interests (see Chapter 4). In a few states, however, including California and Texas, there is still a right of redemption even after the sale. It is important to know what the process and time periods are in each state *before* you invest. There is a complete listing of the current redemption policies for each state in this book's Appendix B. Since these policies change periodically, always check with the county or state tax office.

In some cases, you do actually have increased rights during these redemption periods. In Texas, for example, you are entitled to any rents, leases, or oil/mineral lease revenues during the redemption period, even if the property ends up being redeemed. What this means is that if the owner of the property has a tenant living in it, you can require that tenant to pay their rent directly to you and not to the owner. This means you will make money on your investment, not only when it gets paid off but each and every month you are waiting and the property is leased.

WHAT ABOUT THE REAL ESTATE MARKET COLLAPSE?

It is certainly no secret that the real estate market has undergone and continues to go through some major corrections across the country. Okay, a collapse is probably a better term. So how does that affect your investment, or your decision on whether to participate in this type of investing?

Fortunately, investing in tax liens and deeds is not tied to the ups and downs of real estate cycles. Frankly, there are actually more opportunities to purchase tax liens and tax deeds in a down housing market, as more property owners face financial hardships and are unable to pay their property taxes and their mortgages. Here is another example of how you as the investor can benefit from owning a tax lien certificate in a depressed real estate market.

> You bought a tax lien certificate on a property in Florida for $5,600 at 16 percent interest in a bid-down auction. The owner defaulted on the mortgage to the bank, and no payments have been made for the last year, which is why the taxes didn't get paid—there was no money in the escrow account. The property was purchased by the current owner only three years ago for $275,000, but now they are trying to sell it for just what they owe on the mortgage: $213,000. Unfortunately, it's

been on the market for over a year and they haven't received a single offer since there are other foreclosures in their neighborhood.

Time goes by, and finally the lender forecloses on the property and gets title to the home. But the delinquent taxes don't go away; they continue to accrue. One day, the lender finally gets the property all fixed up, hires a real estate agent, and sells it for $175,000. However, before title can pass to the new owner, all the taxes have to be brought current. At the closing, the past due tax bill is paid to the county, complete with interest, penalties, and fees. Of course, unknown to them, you hold a tax lien certificate on the property, and a week after closing, you receive a check directly from the county, complete with interest on your money. Here's how your check breaks down:

$5,600.00	Tax certificate
$1,344.00	18 months interest
$6,944.00	Your check!

The property owner, the bank, or anyone with an interest in the property, had the right to redeem the tax lien interest at any time. Since redemption can also include not only the back taxes owed plus interest, but also fees, costs, advertising, maintenance, recording fees, and even sometimes your personal costs, it can get very expensive to redeem a property. If they hadn't redeemed, then you could have gone ahead and foreclosed on the property in the third year. Nice investment, secured with a $175,000 piece of property!

Now that you're starting to get an idea of how lucrative this can be, you may be asking "Why haven't I heard of this?" or "Why isn't everyone doing this?" Both good questions, and the answers are pretty simple. People just don't take the time to investigate something they are unfamiliar with, or they believe that when something sounds too good to be true, it probably is. This stops them from doing basic independent research, and realizing just how easy and lucrative these types of investments can be.

People are also afraid to take chances. Have you ever had an idea and said to yourself, "Man, if I marketed that I could make a million dollars"? Then what did you do? Probably nothing and went on working your normal job. Then all of a sudden you're sitting at home watching TV and there's someone selling *your* idea on an infomercial and you are sitting there screaming like a lunatic, "That was my idea!" So what made that person different from you? They saw an opportunity and acted on it. Most people don't, and that is why investing in tax liens can be so lucrative. Be the person who doesn't just read about it, but actually goes out and does it!

WHAT MAKES THESE TYPES OF INVESTMENTS *ZERO RISK*?

There has to be some risk in this, right? As I previously pointed out, there is an inherent risk in anything, even crossing the street. The trick is to conduct your research and due diligence to minimize risks to the point where they are *virtually* zero. But when you compare them to other types of investments, the advantages quickly become clear.

Tax lien and tax deed investments are much better alternatives to investing in stocks, bonds, and mutual funds because they are more certain and more consistent. Second, there are no middlemen, and no commissions for stockbrokers or mutual funds, so all the profit is yours. You know your investment is safe because you are dealing with the government, and it's secured by their taxing authority. With a tax lien, you can determine exactly how much profit you are going to receive from the interest and penalties when the property owner redeems the property, and if the owner does not redeem it within the statutory period, then you can foreclose and acquire ownership at a deep discount. When you purchase a tax deed, you already know you are purchasing a property for pennies on the dollar with equity.

There is a saying in real estate investing that if you are doing it the right way: "You make money on a piece of property when you *buy* it, not when you sell it." Let me explain. When you purchase a stock, you have no idea what it's going to do in the future. You hope it's going to go up but you can't be sure. All you know is that the stock is worth what you paid for it today. But with real estate and especially tax liens, you can buy property with a built-in profit. If you buy a tax lien for $5,000 on a piece of property that is worth $100,000, you already know exactly how much money you can potentially make on this investment. You have locked in your profit when you bought it. You will simply collect your profit when you sell it.

But of course there are some drawbacks. Your investment funds will be tied up for a while. This is why we call this a *get-rich-slow plan*. Yes, there are other risks if you don't know what you're doing; we will address the majority of those in Chapter 6. We also hold regular Internet conference calls that are open to the public, so you can hear from professionals and experienced investors about how to avoid risks and get them down to practically zero.

Are you a gambler? I hope not when it comes to investment funds and your hard-earned money. Gambling contains risks. But think about a blackjack player in Las Vegas who holds a winning 21 hand. If you are that player, you know that your bet has zero risk, even if the dealer also has 21—it's a push. If the dealer busts or has a hand value under 21, you win and receive a high rate of return on your bet. Wouldn't it be nice to be able to see your cards in advance so you could know that you were going to be dealt a 21? Investing in tax liens and tax deeds means the deck is stacked in your favor. With odds like that, it's hard to think of any reasons why not to invest in them. *So, what are we waiting for? Let's dig in and get started!*