

CHAPTER

# 1

## *Getting Started*



It always sounded like a great idea, didn't it? Owning a vacation home. You heard your friends talking about the possibilities. "It pays for itself," they said, and that part of it really appealed to you. After all, it only makes sense. Why spend thousands of dollars on hotels when you can own the vacation home of your dreams, spend as many weeks as you want every year enjoying it, then rent it out the rest of the year, and rake in all that income. Well, I'm here to tell you that you've made an excellent decision. But (you knew there would be a "but") don't delude yourself into thinking this will be simple, easy, or without risks. You need someone to guide you through the process, to show you the ins and outs of how it all works, the pitfalls to avoid, and how to earn maximum profits. If you do things the right

way—by educating yourself before jumping in blindly—you will be much better off in the long run.

The first question you need to answer is this: are you buying a vacation property for your own personal use or for an investment? Before you answer, I want to let you in on a little secret: you can do both! In fact, people who otherwise would not be able to buy a vacation home can indeed if they learn the right techniques of renting by owner. This is not for the wealthy only, and it's certainly not a get-rich-quick scheme. It's a time proven strategy that almost any middle-income family can use effectively. I will show you how your property can pay for itself (see "break-even formula" in Chapter 3). It's not as difficult as you might think. My goal is to teach you how to own a vacation home that will be a financial asset rather than a liability.

Think of this new venture you're embarking on as a unique hybrid. You're marrying the idea of owning a vacation home for yourself with the idea of renting it out to others and keeping it as a long-term investment. So, when you do decide to move forward, the decisions you make will be both financial *and* emotional. Remember back when you bought the home you live in now? Was it just a financial decision? Of course not. You knew that everything had to be right, had to have a certain feel to it before you took the big plunge and made an offer. The location was a key, for sure, but there were other factors: the number of bedrooms, the size and condition of the lot, the garage, the basement, fireplaces, the kitchen cabinets, the wallpaper, paint . . . the list is almost endless. But all of these things mattered tremendously to you, because, after all, this was going to be where you lived, the place you came home to after a long day's work to unburden yourself and relax, the place where you entertained friends, and, quite possibly, the place where you raised your children and gathered your family for holidays for many years. So a lot more went into your decision than just the asking price.

It's much the same when it comes to buying vacation property. A lot of thinking has to go into it. And while it's true that you spend a

certain amount of time planning your vacation trips (deciding on the best airfares, hotels, rental cars, etc.) don't think of buying a vacation home as simply a minor extension of that process. It is, in fact, an entirely different process. It's not just a one-shot vacation where you go for a week, hopefully have a good time, and then head home. Not at all. Buying a vacation home, whether for an investment or for personal use, usually means a long-term commitment. And, if it is for personal use, the stakes are a lot higher. It becomes more than a simple matter of what kind of return you get on your investment. Whatever you do, don't think of this as similar to dabbling in stocks or any other kind of investing. Instead, think of it in the same terms as when you were buying your primary residence. I know you won't be living there year round, but in all likelihood, you will still be making a large emotional investment in this property. It is not just some impersonal hotel where you hang out for a little while, and then you're gone. This is the place you'll be going for that much needed rest and relaxation over and over again every year, probably several times each year. Its location, size, and condition are important, serious issues. These decisions cannot be made lightly.

Try to cover all of your bases. What about personal emergencies? What if there is a major problem with your primary home (the septic system goes, you are flooded, etc.)? What if you or your spouse loses a job? It's not an unrealistic possibility in today's hard-to-predict economic environment. For the most part, there is no such thing as a stable job these days.

I'm not asking these questions to scare you. I just want you to go into this new venture with your eyes wide open. But there's no reason to worry that this is somehow the equivalent of going to Vegas and betting your life's savings at the craps table. Far from it. Here's what real estate expert Jack Simpson said on the subject, "Trying to eliminate risks often creates other risks. Some people put all their money in a 'safe' insured account only to see their buying power taken away by taxes and inflation. Ask yourself, what is the worst that can happen?"

To me, the worst thing is seeing your life slip by without risk and reward. That's sad."

Are there challenges to owning a vacation home? Yes, and they will vary greatly from one person to another. Be sure to bring your family situation into the picture. Do you have children? Do you or your spouse have demanding jobs? People are so busy these days, many of us don't even have enough time to mow one lawn, never mind two! Even if you hire landscapers and other helpers (and the money can add up fast) to assist with maintaining the property, when it comes right down to it, you, as the owner, will still have to spend at least a few weekends a year at the place making sure everything is in proper order. Do you have that kind of time? Even if you do, is that something you're *willing* to do? Maybe you're just too darned tired to spend your time that way. Be honest with yourself about these things before making any decisions. I'm sure you've heard the term "sweat equity." Well, it really plays an important role when it comes to owning a vacation home and renting it yourself. This is something you have to rely on yourself to do. Nobody else can do it for you. Size up the situation carefully before taking the next step. The challenges are not by any means overwhelming . . . *if* you have the right information for dealing with them, which is why, in the following chapters, I will arm you with all of the facts you will ever need to know about vacation home ownership and renting by owner.

Well, I see you're still reading so you must have decided to keep going. Good. Remember, this is supposed to be fun, even though it involves hard work. But if you've gone this far, you're ready to answer another very important question: where will this vacation home be? The old real estate cliché—"location, location, location"—is extremely pertinent at this point. Don't jump to an overly simplistic conclusion such as, "Well, I live in Michigan, and I hate these horrible, snowy, freezing winters we have every year. I'll buy a vacation home in sunny south Florida where I can escape with the kids every February vacation. Man, that'll be the life!"

Well . . . maybe. Then again, maybe not. Have you really thought that plan through? You're talking about a trip of over 1,000 miles. You can't get there easily by car. Every time you need to visit your property, for any reason, chances are you'll have to fly. And while there may be lots of cut-rate airfares these days, it's still not cheap, and it's certainly not convenient. Getting a direct flight can be nearly impossible. Tedious layovers and connections, not to mention all of the post-9/11 security hassles and long lines, can leave you exhausted well before you even arrive at your home away from home's doorstep. Is that what you want? I'm not exaggerating. Having a vacation home in some exotic locale far from home may have a strong appeal, but it's not too practical. I recommend limiting your prospects to places within a six-hour drive of where you live.

You also need to do a good deal of research about the location before making a selection. It's not like you can throw a dart at the map and just take your chances. Even if you're buying the vacation home primarily for personal use, you have to know and understand the market. Just because it is located on a beautiful lake or has a breath-taking view of the ocean, doesn't necessarily mean it is a good deal. What is the rental history of the house? What is the competition like? Is the area glutted with vacation homes? How long is the busy season? These and many other questions are crucial to ask—and answer—before you make any decisions. Do your homework!

Again, personal choices will play a large role. Think about the vacations you have taken for the last 10 years. Actually, write them down; it will make it easier to keep track of things. Where did you go? The mountains? The oceans? The woods? Did you go to quiet places? Somewhere you could lie in a hammock all day and read a book? Or, exciting places with lots of nightlife and fun attractions to visit? Now imagine you had to choose just one of those locations, and that is where you will, from now on, be spending your vacations. Does anywhere in particular come to mind? Hopefully, this winnowing

process will give you some clues as to the kind of places you should be searching for.

OK, so we've gone through the preliminaries: your motivations for buying, and whether your circumstances make this a sensible move for you. Let's assume you've determined that vacation home ownership is indeed the right way to go. Now you have to get ready for the long haul, which means you need to come to the realization that this is a long-term commitment. This isn't the kind of deal where you are going to do a quick flip, i.e., invest a little money, make a few improvements, and cash out way ahead of the game. I'm not saying that it can't be done, and in some cases I've seen people do it quite successfully. But for the average vacation homebuyer, that is not going to be the route you take.

Instead, you should look at it this way: the investment that you'll be making will enable you to afford a property that you couldn't otherwise afford. The one constant in real estate is that it almost always appreciates, and sometimes it does so very quickly. If you play it smart, you may build up a good deal of equity in just a few short years. Yes, at first you might have to rent it out for most of the year just to break even. It probably won't be a cash cow, so don't set your expectations too high. However, with a little patience, as the years go by and the equity continues to build and rents increase, you will be able to rent the property less often and still stay ahead of the game. It will eventually become profitable, and in the meantime, you have a wonderful place where you can spend your future vacations. No reservation required.

Before we go too far, let me add a word of caution. They say politics is the art of compromise. Well, the same could be said of the real estate game, especially when it comes to vacation home ownership. We discussed earlier how this is not only a financial investment, but also an emotional investment. In other words, you have to really like the place before you go ahead and sign on the dotted line. And while that is certainly true, liking the place isn't the same as *loving* it. Yes,

you want to be satisfied with it. You want it to be a place you are proud of and eager to visit. But you have to be realistic and acknowledge that sometimes you can't have everything that you want. For example, let's say you have a large family, and you really have your heart set on a five-bedroom house. However, through your extensive research of rentals in the area (see, you're taking my advice already), you've discovered that three bedrooms rent much better. Time for a compromise. Buy the three-bedroom (some of the kids will have to share, but they'll survive just fine), and put yourself in the best possible position for renting. Go with the situation that will really keep the cash flow up. The same thing happens when it comes to issues such as buying a furnished or unfurnished place. The latter means more work, of course, but in the end, it could be worth it. Explore all your options, and you will be glad you put in the extra effort. Compromises such as these will be necessary every step of the way—beach vs. just off the beach, condo vs. house, and many others. Just be prepared for these compromises, and you will be more likely to make intelligent, well-informed choices.

The bottom line to all of this, and a good credo to keep in mind as you begin this new adventure, is . . . you must be an actively involved owner! Get all the facts. You have to know what exactly it is you're buying, what the competition is, and who your potential renters are. This background work is well worth the effort because you'll soon be enjoying a vacation home that pays for itself. You may very well turn a profit. But, you must do your homework first. So keep reading.

Note: When people start considering the idea of buying vacation property, some people immediately think "timeshares." Let me say that that assumption is false. That is not what this book is about and, in fact, I see many disadvantages to timeshares and very few benefits. Think about it. When you buy a vacation property, you own it 52 weeks of the year. With a timeshare you only "own" it one week of the year. To me, that doesn't seem like true ownership. Moreover, they have no resale value at all. Let's say you buy a timeshare for \$50,000. If you bought it for the whole year, what would the cost be? Do the math: 52 weeks

x \$50,000 = \$1.3 million. Now take a close look at the property. Do you really think it is worth \$1.3 million? I'm willing to bet it's not. You could probably buy a similar unit down the street for \$200,000. So why would anybody get involved with this whole concept in the first place? It's usually the result of high-pressure sales tactics, which should be a sure sign right from the beginning that it's a bad idea for the buyer.