



What to Look for When Buying a “Bargain” Property

A Fact Sheet for Owners of Rental Properties

What’s *Really* a Bargain?

“Sure it needs some fixing up, but the rental income should more than cover the cost of repairs. Besides, if I put in a little “sweat equity”, I can make most of the repairs myself.”

It’s tempting. The allure of the “bargain property” has lured many investors into serious legal and financial difficulties. Bringing a substandard property back to profitability is not as easy as it may appear at first glance. Unless expert guidance is available, it should not be attempted by the first-time buyer.

What makes a substandard property appear to be such a bargain at first glance is the fact that the income from rents on the building can often exceed the mortgage payments by a substantial margin. Sometimes the present owner is even willing to help with the financing. The reality is that there is no free lunch when it comes to property ownership. This is just as true for a single-family home as it is for a rental property. A bargain price on a building almost always reflects poor maintenance and sometimes hidden legal problems.

What Do I Need to Know About Purchasing a Bargain Property?

First of All: Is It Really a Bargain? Take a second look at that selling price. Now take a look at the prices of similar properties in the same neighborhood. What might seem like a great price in one area may not be such a great price in another. Remember that property values can move in either direction. Buying at the wrong point in a housing cycle can mean that you end up with a property that is ‘under water.’ Look at the going rents for similar properties in the neighborhood. How much will you need to raise the rents that the tenants are presently paying in order to break even? Is it realistic to do so?

Is This Your First Such Purchase? Renovating a substandard property can be profitable, and it performs a service for the community. But it is most successful when it is undertaken by an experienced property manager – or at least when expert guidance is available to the purchaser.

Housing Codes. One of the most common reasons a property is a ‘bargain’ is that it may well be in serious violation of state and local building codes as the result of deferred maintenance. Inexperienced buyers may be aware of some, if not all, of the problems that need to be addressed in a building, but assume that they can get around to making the necessary repairs at their leisure. What they don’t realize is that these problems usually represent violations of the housing codes, and failure to bring them into compliance within a very limited amount of time can result in fines, lawsuits or even revocation of the certificate of occupancy for the building.



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Among the codes with which all residential buildings must comply are: state building codes, local ordinances and (in the case of rental properties) Chapter II of the State Sanitary Code. If someone under six lives in the property or moves in at some later date, you will also need to ensure that the property is in compliance with federal and state lead paint requirements (see below). If you are considering purchase of a distressed building, be sure to check with local code enforcement officials to find out if the present owner has already been cited for any code violations. Go to www.mass.gov/Eeohhs2/docs/dph/regs/105cmr410.pdf for more information about code requirements.

Making Repairs. When you repair and/or renovate a building, remember that all repairs must be made according to code. In many cases, permits need to be taken out. Also remember that, under the state building code, once you renovate a residential property, it must be done in accordance with the present code. Features that were considered acceptable as ‘grandfathered’ under an earlier version of the code may no longer be permissible once you renovate.

Inspections. Before purchasing *any* property you first should have it thoroughly inspected by a professional housing inspector. This is particularly true with distressed properties. Once you have a complete list of repairs that must be made, obtain detailed estimates for making these repairs. The inspector can tell you which repairs must be made right away and which can be deferred to a later time

Lead Paint. Massachusetts has some of the strictest lead paint laws in the nation. If a building was built before the late 1970s, there is a high likelihood that lead paint may be present. If there is lead paint in a house or apartment in which someone under six resides, the owner *must* bring the property into compliance with state and federal lead paint regulations. The cost of doing this can range between a few thousand dollars and more than \$15,000 per unit. Also, contrary to popular belief, refusing to rent a house or apartment to a family with a child under six because of the presence of lead paint – or even ‘warning’ them that they might not want to rent from you because of the presence of lead paint - is a violation of the law. You cannot ignore the lead paint laws. You do have the right to inspect a property for the presence of lead paint before you purchase it. If the owner of the building you are considering buying says that there are ‘Letters of Compliance’ that certify that the apartments in the building are in compliance with the lead paint law, be sure to confirm that he or she has maintained the compliance from their date of issue.

Zoning Matters. Is the building in compliance with local zoning? Infractions of local zoning requirements sometimes go unnoticed until a building is sold. Among the more common problems that prospective borrowers may discover are: a business that is operating out of a building located in a neighborhood that is zoned as being only for residential purposes, or an attic that has illegally been made into an apartment. A simple check with the tax assessor may often tell you whether the three-family house you are planning to buy is actually a two-family – and whether your anticipated rental income will therefore be reduced by one third.



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Are there Bad Tenants? If there are problem tenants in the building, do not assume that you can readily evict them. When you purchase a building, you are a ‘successor in interest’ to the agreements of the former owner. That person’s tenants become your tenants. Inept landlords sometimes sell buildings to get rid of the problems associated with their tenants.

Are You Even Ready to Be a Landlord? There is a lot more to being a rental property owner than simply picking up a check from your tenant each month. Even if you only have a single tenant, you are as liable for compliance with the state’s numerous laws, requirements, regulations and housing codes as someone who owns hundreds of units of housing. Learn what they say before you decide to buy a rental property. Has the present owner collected and properly handled security deposits and last months’ rents from the tenants? (For that matter, do *you* know what the law says about how they are supposed to be handled?) A good landlord must be a business manager, an accountant, a human relations specialist and an expert in all types of repairs. At the very least, being a landlord is equivalent to taking on a part-time job – and it’s not a job that you can easily walk away from. HAPHousing routinely sponsors classes and counseling in rental property management matters cost-free to participants, as well as making the textbook “Property Management for Massachusetts Rental Owners” available. Before you buy a rental property, you should avail yourself of these services.

Prepare a Budget. Don’t fool yourself with rosy projections. Even a building in good condition has ongoing expenses. Before you can consider bringing a substandard building back up to shape, you must first be prepared to cover such ongoing expenses as: mortgage payments, property taxes, fire and liability insurance, water and sewage charges, utility bills, trash removal, snow removal, and contingency funds for times when unexpected repairs are required, or for covering loss of rent when a tenant moves out.

In the long run, it’s often less costly to purchase a building in good shape than it is to renovate one that is not!



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