CW 818- Insuring rental income with Leaselock, Reichen Kuhl, The Amazing Race, US Air Force Officer, Service members Legal Defense Network, author of Here's What We'll Say

Jason: Welcome to the Creating Wealth Show, episode 818, 8-1-8. Thank you so much for joining me. This is your host Jason Hartman and happy Easter to our listeners in 164 countries worldwide. Thank you for joining me today and gosh, today we are going to talk about yet another interesting and innovative service that is here to help us with our investments and that is Leaselock. This is basically lease performance insurance. It's not really, really inexpensive but, guess what? You don't pay for it. Your tenant does. And at first when I first heard about this company and its service and the way its product worked, I thought, you know why would a tenant pay for that? Why would they pay the money for that insurance? And then I kind of realized we commonly pay for someone else's insurance; it's what we do in the world of mortgages. Not just from one angle, but from two angles. We pay for it in terms of private mortgage insurance or MMI, which is the insurance you get on an FHA loan or PMI that you get on conventional loans and we also pay for title insurance, so it is fairly common for one party to pay for another party's insurance and in this sense the tenant is paying for the insurance that insures the landlord that they will have performance in terms of their rents. So you'll hear more about that in just a moment, but first I want to help you gain a little perspective so let me grab something.

Yes, a couple of papers here are hot of the press, hot off the printer. All right, so the year is 2017 and if you are a faithful, loyal listener to the show I want to tell you first of all how much I appreciate you but, secondly, I want to tell you how smart you are because you are listening to the Flashback Friday episodes and when you listen to the Flashback Friday episodes, you gain perspective. I was talking with one of our clients, Dan, the other day, a great guy. He was talking about the Flashback Friday episodes and the idea of perspective so Daniel, thank you so much for bringing that up and I want to talk about it before we get to our guest today with our listeners a little bit today because here is the perspective. Remember, I got into the real estate business way back when at the ripe young age of 19 years old, in my first year of college, it was just two weeks before my 20th birthday and I got into it because I wanted to be a real estate investor. That whole inspiration. And when I started I started working with just investors. I was placing little classified ads in the Orange County Register and the Pennysaver, yes, that was before Al Gore invented the Internet and before he had invented global warming. Okay, so you've always got to raise a little controversy Jason, yes you do. Okay, so I was placing these little classified ads, advertising government repos and VA repos, FHA repos and HUD repos—these are properties that had government insured mortgages, FHA and VA, Veterans' Administration, and the people went into default and when they went into default, the government got the properties back and then they would auction them off and this was my whole specialty, the beginning of my real estate career as a real estate agent at age 19 and the vast majority of my clients were investors but I did have some first-time home buyers too. And it was very, very interesting working with all of these people as I was driving them around in my little, brand new Volkswagen Jetta after my mom had given me a massive lecture on how absolutely crazy I was for entering into a financing arrangement on my little Volkswagen Jetta to have car payments of… get this… a

whopping $189 per month. Yes, I know, times they are a changing. And now my lease payments on my crappy and I will emphasize that, crappy Tesla are $1640 per month. Yes, the times they are a changing and my first Tesla I paid cash for it but this one I got on a lease. Really, it's better to get a lease, keep the money and be able to invest the money in properties. But, you've heard about my complaints this time around on this Tesla, it's been pretty, pretty darn bad. Anyway, more on that on my Twitter account. You can see videos of me cursing at the car and showing how bad it is. Tesla has seen these videos and they completely deny the problems. Yes, a video, you would think that would be undisputable proof but for some reason Tesla, who thinks they walk on water, they deny the problems. Anyway, for the risk of getting on it, let's not get on a tangent here and let's talk about these properties and let's get some perspective on our real estate investments.

Okay, here we go. Then, fast forward, I'm talking about my career here for a moment so I started doing that and I was at Century 21 in Anaheim and I was selling to mostly investors, some first-time buyers, the homes I was showing were disgusting, completely disgusting. They were usually boarded up so you had to show the house with a flashlight, you had a special lockbox key and you'd walk in the house and the house stunk. It was disgusting, okay. It was really gross. But, my investors back then thought it was an incredible time to buy real estate back then because the interest rates were only 12-14 percent interest. Yes, I know, you think wow that's amazing, right? One of the perspectives I want to make sure you have is the understanding, remember, when people buy a property they rarely buy it based on the price; they buy it based on the payment. Okay, they buy based on the payment. Now, that's one thing to know. The second thing to know is, let's just fast forward here a little bit and let's go to 2004 now and let's talk about the time that I got into the investment only real estate business. This was about a year before I had sold my traditional real estate company in 2005 and I knew I was starting to negotiate that deal and I wanted to sort of set up my next potential career and it turned out to be the investor only business and so I've been in that business ever since, well I could say 2005 when I completely got out of the traditional real estate business and way back in 2004 when the year of overlap, okay, one year of overlap, way back in 2004 when I did my very first Creating Wealth seminar for real estate investors, one of the things we were talking about in 2004, in 2005 is we were talking about rent to value ratio, rent to value ratio. And here's what's really interesting about it. Back then, here was the perspective people had. They thought a property was a fantastic deal and a fantastic buy, a great buy if you could buy that property for a .7 percent RV ratio. Not one percent, not .8 percent, not .9 percent, but .7 percent. They thought that was an incredible deal. And when they looked at the properties, they looked at the performance as we were using realestatetools.com back then, property tracker, the property tracker but the apps were not yet invented. Back then, in 2004 and 2005 we would have had someone brought an iPhone into our lives back then we would have thought it was magic. We would have thought it's a really amazing time to be alive because there was no such thing as an iPhone. So that was before the era of the old smartphones. So there were no apps, apps that you can now get in the app store for iPad and iPhone. There was no realestate.com app. We did have property tracker back then and when you looked at the property tracker and when you looked at the property tracker performa and you saw a .7 percent RV ratio, when you looked at the multi-dimensional characteristics for

real estate investment and you looked at the amount of leverage you could get and you looked at the appreciation and looked at everything back then with very conservative assumptions of not more than 7 percent annual appreciation not less than an 8 percent or one month per vacancy rate and a management fee of around, and this will vary a little bit, at around 8 percent and then maintenance percentages anywhere from two to eight percent back then, okay. When you looked at that, you would generally get a total return on investment somewhere in the 20 to 30 percent annual range. Now, nowadays it's getting very challenging to get that coveted one percent rent to value or RV ratio, right? You all know how difficult that is. So, like the famous song, if you can't be with the one you love, then love the one you're with. I always thought those lyrics were really funny. By the way, since we're talking about relationships here for a moment, there's another great relationship song that can teach us a lot about relationships. It's by a band called 38-special. You know the song I'm talking about, don't you? Yeah. Hold on loosely but don't let go. That's great advice, okay? That might also be good advice for investors nowadays. Hold on loosely but don't let go, right? Because if w cling too tightly to our old ideas, we're gonna lose control. Boy, I'm actually doing that pretty well just like in real estate investment—thinking of that famous 38-special song, aren't I? Okay, so the old idea was that we would get one percent rent to value ratio or even better 1.2 percent, no and I hate to totally bum you out here but you know that during the ugliest part of the great recession when very few people had the confidence and the vison and just the sheer raw guts, the kahunas, as they say, by the way, what is the actual translation of that word, kahunas. I'd have to look that up if I knew how to actually spell it, I would do that. Anybody had the confidence, the guts, whatever, the hoostba. How's that one? The hootsba to invest in real estate during the depth of the Great Recession, they sometimes got rent to value ratio… you ready for this… 1.4, 1.6, even 1.8 percent. Yes, they could buy a property, in just in round numbers you could say the property was cheap. No, it wasn't. They'd buy property for $100,000 and the total rent, now this is a multi, this is a plex. By the way, we've got to stop calling these duplexes, tri-plexus and four-plexus, multi-family. I know, a lot of people refer to them that way. When I think of multi-family, I think of more than four units. I think we need to classify these two, three and four unit properties as plexus. It's a plex. It's a duplex, tri-plex or four-plex. So that was a plex, and this plex for $100,000 could literally rent for $1600-1800. I know. I'm bumming you out. I get it. And nowadays, a $100,000 property that rents for $1,000 you're doing great but just remember when you gain some perspective and stop looking at the metrics that don't tell the whole story, what metrics are those? Well, the first offender is cap rate, that's a big offender. Why is the capitalization rate such a big offender and a misleading metric? It's really misleading because it doesn't include appreciation and it doesn't include leverage. But there's one more thing it doesn't include because leverage and my own metric, the one that I have… well, I didn't make it up but I did discover it and I popularized it and if anybody else is talking to you about it, they're copying me. I just want you to know that but hey, imitation is the sincerest form of flattery.

There is this one weasel in our business, drives me crazy. He just relentlessly copies me. I mean, it's really just unbelievable and one of our client's who's probably listening right now said they heard him on this podcast and it's just like he copied my ten commandments. There you go. Imitation is the sincerest form of flattery. But the other metric that cap rate doesn't consider, of

course, you know what I'm gonna say probably if you're a regular listener—inflation induced debt destruction. Inflation induced debt destruction is not considered there. The other one you really got to be careful of, you've got to stop looking at so much is cash return. Now, look it, I'm not saying you shouldn't consider these metrics. I'm just saying that they don't tell the whole story. I mean, why do you think that income property, the most historically proven asset class in the entire world, why is that? It's because it's a multi-dimensional asset class and as such, you earn your return on investment from so many wonderful sources, so many ways to get that return on investment and if you look at cash on cash return or cap rate, you're not looking at the whole picture and it's really dangerous not to look at the whole picture. Look it, you all remember that tragic incident where JFK crashed his airplane on a foggy night on the way to Martha's Vinyard, right? Because he only had 120 hours of flying experience and the maximum number for a pilot, if you're a general aviation private pilot is about 200 hours, 200 maybe 250 even. That's when your insurance rate will drop a lot as a pilot, okay. If you're an inexperienced investor, you're going to look at information that doesn't give you the whole picture, but if you're experience or even if you're not experienced but if you gained experience from someone like hopefully yours truly, you have learned you must look at the whole picture. See, JFL Jr. crashed because he wasn't looking at the whole picture. He didn't know how to be an instrument pilot. He was looking out the windows, all right, and that wasn't the whole picture. Because when you're in an aircraft it's very easy to become disoriented. I mean, one of our Venture Alliance members, Brandon, is a fighter pilot, he knows there's a lot more to the picture if you will… I shouldn't even be calling it a picture because that implies that it's visual only and just looking out the windows of your cockpit, right? There's way more to it than that and so JFK Jr., of course, just crashed right into the ocean. Okay, right into the water because he didn't see the whole picture because he couldn't without understanding how to read his instruments. So, our instruments we use as real estate investors, they are the performa. We've got to understand how to read the performa and to do that properly we must look at total return on investment. Total return on investment. Now here's two quick examples and then we'll get to our guest. And these are right off our website right now. These properties do say they're for sale, however by the time you hear this, one day from now, they may be gone. And you understand that it is a fast-moving market right now so it's very important that you work closely with your investment counselor. They can find you good properties.

All right. Here's one and this is Indianapolis. $159,900 and with a 75 percent loan to value and it does not get you a one percent rent to value ratio. Projected rent here is only $1,400 and your overall return on investment, though, is projected at 27 percent annually… 27 percent. Folks, people who understand the concept of perspective in the world always ask themselves the question. Are you ready? Here's the question: compared to what? Compared to what? 27 percent return on investment. That's the projection right here on the performa. If you only look at cap rate or cash on cash return, you'll do this. You'll throw that property away. You'll miss out, okay. Here's another example and this property is brand new. It's in Jacksonville, Florida. Here it's $164,900. Projected rent is only, yeah, I'm saying only because it's not one percent… $1,375. Overall return on investment on this performa, 29 percent annually. So you know if it only goes half as well as expected you're going to get 14.5 percent. Where are you going to beat that?

Where are you going to get 14.5 percent? And that's on the bad scenario. That's on the scenario that says it only goes half as well as the performa. All right, look it, folks. Income property's the most historically proven asset class in the world and there is a reason and the reason is that it's multi-dimensional and it offers, like we talked about before, a lot of flexibility that allows you to choose the dynamics of your investment later by refinancing it, selling it, leasing it, 1031 exchanging it. You've got so many options down the road so the scenario you buy it today does not lock you in. Even though that's a pretty damn good scenario. It's pretty good. Now back in 2004, let me enlighten you with one other thing. And this is why it's important to listen to the Flashback Friday episodes because back in 2004 I told you that the ideal rent to value ratio was . 7, .7, all right. But guess what the acceptable rent to value ratio was for people back then. Ready? .5, .5, half a percent. In other words, the $150,000 property would only rent for $750 a month. Now listen, I don't think that .5 is good. I'm just telling you that people that were doing nationwide investing back then were ready, willing and able to purchase lots of properties at .5. And you know why? I'll tell you why. Because the questions they asked themselves was compared to what? Compared to what? If they were to be investing in the socialist republic of California or in Miami or Boston or New York or Washington, DC or any, you know, these are just examples I give, there are several others. Any expensive market, if they were in the Pacific Northwest… we used to do Redmond, Oregon. Okay, that was one of our markets. It's just outside of River Bend and I was talking to someone just a few weeks ago and he was telling me all about the market there and it's just way too expensive now. What about our clients that invested there? The RV ratios are no good anymore. I mean, the rent for what I paid for it in 2005 is pretty good but the rent to value is not very good and that's why we help rebalance your portfolio. Portfolio rebalancing. That's what our investment counselors are here to do with you. So, as usual, I've gone a little long here. What's new, right? You're used to that. I get off on a tangent and I think what am I going to talk about. Here we go, 24 minutes in and I'm still talking. It's time for me to shut up. Let's get to our guest. I really do want you to hear this innovative offering that's available to you. So check it out. I think I asked all the right questions of our guest. This is just another one of those things, maybe you don't use it, maybe you just put it in the back of your mind and someday, with some property you have, one property in your portfolio or maybe three of 20 properties in your portfolio could really benefit from something like this. So, it's just an option and that's what we want to do. We want to tell you about the innovative things that are going on in the industry so this is one of them. May or may not be applicable but worth considering so be sure to go to Jasonhartman.com to check out my educational products to be sure you are taking advantage of the 27 minute video that's free on the front page of our website Jasonhartman.com and that will help you analyze real estate deals. All right. Here's our guest as we talk about renter insurance.

It's my pleasure to welcome Reichen Kuhl to the show. He is CEO and founder at LeaseLock. He's an attorney, a season 4 winner of the Amazing Race, former US Airforce officer, spokesman for service members legal defense network and author of the bestselling book Here's What We'll Say Growing Up, Coming Out in the US Air Force Academy. Reichen, how are you?

Reichen: Hey, thank you. Thanks for having me on the show. I'm great.

Jason: It's good to have you on. You know, I love talking about these innovative products or services in this case for landlords, especially for landlords that are self-managing, you know, they just want to have some more security and your service is interesting. I found it quite a while ago actually and I wanted to get you on the show to talk about this. So LeaseLock is basically an insurance policy that insures tenant performance. That the tenant will pay the rent. Wouldn't we all love that as landlords, right. But it does cost a little bit of money—it's paid for by the tenant, now think about this. At first I, Reichen when you were first explaining that to me, I thought you know how is the tenant going to be willing to pay for this but if you think about it when someone gets a mortgage and they need to have either MMI mortgage insurance on like an FHA loan or PMI insurance on a conventional loan, they pay for the mortgage insurance, the borrower pays the mortgage insurance. With title insurance, at least in most cases, I believe, the lenders policy is paid for by the borrower, so here the tenant is paying for the landlord's insurance benefit, right?

Reichen: Correct. And in those cases, for like PMI insurance the reason that those people pay is a lot of times because it's mandatory and our landlords that were working with now at LeaseLock and a lot of our property management companies are making the LeaseLock option mandatory. The landlords have decided, along with us, that the old way of adding extra security deposits you just have a big pile of money sitting there that will protect you for a month or two, or asking for a resident to go get a cosigner isn't the answer. And the real answer is make the resident go get insurance on the lease so that if there is a default the landlord is always indemnified and only in that case will they rent to that renter preventing risk.

Jason: Okay, so you wouldn't do this with every applicant, right? You would only insist on it with a marginal applicant… like what would you do if the FICO score is above or below a certain number or income, or how do you actually implement this without being accused of discrimination? That's what I would be concerned about.

Reichen: It's up to the landlord. They always have their standards set so they say this group of people who meet their financial credentials are approved. Those who do not meet the financial credentials are denied, and this group of people we actually want them if they provide security to us in the form of a security deposit or a cosigner. That's the group that we help so the landlord pushes that conditionally approved group over to LeaseLock and then we take it from there. We have a lot of student housing and property management companies who make LeaseLock mandatory for everyone. So everyone in a student housing complex has to have a LeaseLock on it. They don't care if you meet the criteria or not. They want everyone to have it so if anything goes wrong they know that they're protected by the LeaseLock insurance.

Jason: Okay, but we both know that student housing has been a bit of a unique animal because a lot of times the students want to rent the property and they have either no credit score or very little credit and maybe the parents won't cosign, but even if they do cosign they might be

marginal themselves in terms of being qualified so take us through the mechanics of how it works. Do you, for example, do the tenant screening on your end? Do you order the credit report or does the landlord do that completely separate from you using whatever service they want.

Reichen: Yeah, I'm going to give you a lawyer answer and the answer is it depends. So it depends in the landlord. Some of our landlords have decided they want everybody on a LeaseLock and can they push everything over to LeaseLock to do and the kind of screening that we want to do but most landlords do their initial screening and accept the applicants who meet their screening criteria but when they have their conditional applicants that they send to LeaseLock, we also go through kind of a super screening process and we take a lot more information from the renter. Because of the technology we have in order to look into bank statements, past rental history and also employment and payment history from that employer, we'll make a decision usually within 24 hours on that renter to tell the landlord, yes, we're going to go ahead and apply an insurance certificate on this landlord. We don't just base things on credit score. We found that credit score is not really a good indication of who is a rent payer but LeaseLock cares about who is a rent payer not who has perfect credit. So you could be late on your credit card bills and late on your car payments but if you're a rent payer we're definitely going to issue a certificate for that person so that's what we're leaning toward, looking to see that risk. You know, your typical landlord screening is looking at income and credit score and that's not really the best indicator if someone's going to pay their rent.

Jason: You are so right about that. Let me just mention that. I've been searching and studying this a bit. Do you know there are so many data points that determine whether someone will pay either their rent or their car payment because what we find in credit scoring is so many… some may say screw you I'm not paying my debt collectors but pay the rent on time. And interestingly, there have been studies for people who, for example, when they fill out credit applications online, if they do it in all caps versus upper/lower case, they have determined those people are less likely to pay on time. There's crazy stuff, it's getting really good. It's getting super interesting.

Reichen: We're able to screen the way people spend because of our access to banking accounts and spending habits. We do some crazy analysis in the office on our data. We can link the likelihood that someone's going to pay rent to how much they spend on let's say eating out, where someone who's eating out all the time, expensive meals, they're going to be in a different group of renters than someone who spends a little money on a lot of meals. It's interesting. We can run all kinds of analysis and it's really part of our secret sauce to be able to determine, okay, we're going to look at everything about this person, their habits, their income, where they live, what part of the country they're in, male/female, we can look at all that stuff because we're allowed to look at insurance risks and a lot of those things that are protected classes, those are still factors in determining risk. It's interesting what we can do and how we can determine it.

Jason: Well, okay so a couple of interesting things that you said there. Do the big meal spenders pay better or worse than the people who spend a little bit but have a lot of meals out?

Reichen: People who tend to spend a lot and splurge a lot more are people who are not as aware of how much they have on hand at any one time and so as people who are just dipping a little bit and constantly paying attention to how much they have, even though they're spening the exact same amount of money they're just people who end up having to pay their rent at the end of the month because they're monitoring it better.

Jason: The splurge mentality is live for today, tomorrow be damned, and so that's the thing and so when the first of the month comes around and the rents due, they don't have it.

Reichen: Exactly.

Jason: Another interesting thing that you said in fair housing laws, we all have to be very conscious of protected classes and look at that differently.

Reichen: You're allowed to look at those kinds of habits, I mean obviously, you're not allowed to just blanketly deny insurance or services or nay kind of product based on race or gender but we can certainly look at those things and add them into all of our predictors and be able to kind of decide what our entire risk is going to be for the company and go from there. But you're right, you always have to provide at least the same opportunities for everybody. But for predictors, yeah, all these planned but we do have to comply with fair housing law in ways where we don't want to deny housing to someone who would otherwise get it but the cool part about LeaseLock is these people who are coming to us are already being denied and so we can only bring them above that level so they're either going to be where they were when they came to LeaseLock and be denied money unless they can come up with housing where the LeaseLock fee is going to be way lower than that or they're going to have to find a cosigner. We say we take B renters and turn them into A renters for the landlord.

Jason: Okay, so talk to us about how much this insurance is going to cost. I'm aware of the prices but explain how it works.

Reichen: The base rate is 10% of the full lease value. To keep it simple, let's take a $1,000 a month lease that is 10 months long. That's going to be a $10,000 lease value so seven percent of that $10,000 is going to be $700 so that's what the renter is going to have to pay upfront in order to have us issue an insurance certificate to their landlord saying that we will indemnify for all lost rest. The renter only has to pay half of that upfront so they would pay $350 upfront and with that $350 payment we'll go ahead and issue the insurance certificate to the landlord that says if you miss out on any throughout this lease we're going to indemnify you, if the renter skips we're going to pay the rent while the apartment is empty for the whole time until you re-rent it or the lease is over, whichever comes first, then we're going to take the rest of the payments from the renter back account or credit card for the next five months.

Jason: You gave an example of a 10 month lease, I know you're used to that because you probably deal with a lot of rental housing and most housing nowadays is just your year-round leases, but the point here is it's the amount of the lease.

Reichen: Correct and what we're competing with is the landlord saying well we want you to put an extra security deposit of one month's rent.

Jason: And so in that case it would be another $880 dollars.

Reichen: It would and we find that most of our renters who are coming to the LeaseLock program, they don't care, they care so much less about putting the money down and getting it back in a year than they do about what is the cheapest absolute moving cost that I can get right now to get in an apartment taking the least amount of money out of my bank account. And that's what we appeal to. We appeal to the renter going hey landlords love it too because the landlords say keep it cheap for them because I'd rather you push them because them I'm indemnified for the whole lease instead of one month's rent. We even cover eviction fees with lawyers and courts. So insurance is the better option. It makes more sense than the antiquated way of collecting security deposits and looking for cosigners that you're probably never going to find and if you do, they're not going to pay.

Jason: Okay, interesting. Is there anything else you want people to know? Do you have any other products or services?

Reichen: Nope. That's about it. We're keeping it simple for now. We realize maybe down the road we can do other kinds of programs but right now we're really focusing on this one market or this one industry of rent protection and we want to become the best in the world.

Jason: Do you have a competitor?

Reichen: We have competitors but we don't have any competitors who are nationwide. There are some working with surety bonds and some who are working in only regional markets. We have under our portfolio the largest property management company in the country and then several under those. We pride ourselves in being the trusted name and the trusted company in the industry so we watch our competitors and we always strive to do better.

Jason: How long has LeaseLock been around?

Reichen: I wrote LeaseLock on a napkin in 2010.

Jason: Hey, I've got to ask you one more question. Are there any perimeters, you know will you not rent to the bottom of the market or the very high end market. You know this is not an area most my listeners are in but I want to get the question out there before you go. You know,

someone has a $300 a month unit that they want to rent and get this insurance on. Can they get that through LeaseLock.

Reichen: Yes, we will do that. Where are perimeters really are for renter risk, we do stop at a credit score of 490. We don't go there and we just can't help everybody. As far as high as we'll go, we've gone really high because it's based on the lease value and so the lease fee is going to be a lot higher.

Jason: So if the rent is $15,000 a month or $180,000 a year, you'll insure that lease too but that would be pretty expensive insurance.

Reichen: We'll do it but if you can buy the LeaseLock, we'll do it.

Jason: And if it's a $300 a month place, you'll do that too, right?

Reichen: Absolutely.

Jason: Interesting. Hey, I know you've got to run. The website is LeaseLock.com, anything else you want to say?

Reichen: No. I just want to thank you for having me on the show and letting me talk about this company which I'm super proud of.

Jason: Yeah. It's a pleasure. We love to bring new and interesting and innovative ideas to our listeners and this was one of them. Thanks for joining us.