

Lease-Options

What is a Lease-Option?

A lease-option is a combination real estate rental, sales and finance technique. It is a property lease for a fixed time period, such as 12 or 24 months, with an option for the tenant to buy the property at an agreed option price during the lease term.

Buyers like lease-options because little up-front cash is required. Sellers also like lease-options because they provide necessary cash flow to pay the mortgage and property taxes from a tenant who has a vested interest in treating the property well and who is likely to buy it.

The Biggest Lease-Option Obstacle

The biggest obstacle to a lease-option transaction is often the realty agent. The reason is the agent receives only part of their commission up-front at the time of entering into the lease-option.

The commission balance is paid when the option is exercised. Many agents who can't afford to wait for part of their commission don't realize a lease-option is better than no sale at all.

Advantages For Buyers

Lease-option benefits are not one-sided. Advantages for buyers include:

- **Small Amount of Up-Front Cash Required**
The amount of up-front cash required to acquire a home or other property on a lease-option is usually small, often just a few thousand dollars for the first month's rent plus non-refundable option consideration. This option money is in lieu of a security deposit.
- **Monthly Rent Credit Builds a Down Payment**
The unique characteristic of a lease-option is the rent credit toward the buyer's down payment. Typically, the rent credit is 10 to 100 percent of the monthly rent, depending on how motivated the seller is to sell. The higher the rent credit percentage, the greater the probability the tenant will buy.
- **Try Out the Property Before Buying**
Another special lease-option benefit for the tenant is the ability to try out the property before buying. If it is undesirable, the tenant hasn't tied up a large amount of cash in a home that might be difficult to resell.
- **Control Property With Very Little Cash**
The ability to control a property and profit from its market value appreciation with very little cash is called leverage. Lease-option buyers have this unique advantage.
- **Longer Terms Mean Greater Profitability**
Although most residence lease-options are for short terms, such as one or two years, smart investors seek lease-options with the longest possible term. They reason the property is likely to appreciate in market value over the long term.

Advantages For Sellers

Unless your property is located where there is very strong demand from buyers, lease-options can be especially advantageous for home sellers.

- **Strong Demand From Prospective Buyers**
No matter how slow the local real estate market might be, there is almost always a strong demand from lease-option buyers. Many prospective home buyers can usually afford the monthly payments but they have often had insufficient cash for a down payment. The lease-option solves this problem by giving the tenant-buyer a rent credit toward the down payment. It's like a "forced savings account." In addition, the tenant-buyer usually pays up-front nonrefundable consideration for the option, typically several thousand dollars.