INVESTOR FIELD GUIDES / BOOK 06

Flip or Pass?

Protecting your profit before you buy, while you renovate and when you sell

Real Estate Nate

Free Investor Academy

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The properties, amounts and situations in this guide are hypothetical. They are not Nate's past transactions or a prediction of your result.

Start at the exit

Before I get excited about a low asking price, I want to understand who would buy the finished home, what they can reasonably pay and what it will cost to deliver that property. A flip has more moving parts than purchase price and repairs. Financing, insurance, taxes, utilities, selling expenses, time and surprises all have to fit inside the deal.

I do not want to discover at closing that a profit existed only because I forgot a cost. I also do not want to use the highest possible resale price just to make the offer work. My goal is a defensible offer with room for a difficult outcome.

1. Support your finished value

Review recently closed comparable sales with similar location, size, layout and finished condition. Look for differences that a buyer would care about: a busy street, a missing bathroom, an unfinished basement or a superior lot may change the comparison. Active listings tell you what sellers are asking; closed sales help show what buyers actually paid. Neither should be used without checking its relevance.

Your after-repair value, or ARV, is tied to a scope. A $200,000 comparable that received a full kitchen, updated systems and professional finishes may not support a $200,000 value for a home receiving only paint and flooring. Estimate a range, document why each comparable belongs, and investigate the differences. If the project works only at the top of the range, recognize how much depends on that assumption.

2. Budget the entire project

Assume a hypothetical resale value of $200,000. You estimate $35,000 for the defined repair scope, $5,000 for a separate repair contingency, $25,000 for acquisition, finance, holding and resale costs, and $25,000 as your required pre-income-tax profit. If those illustrative costs stay fixed, your purchase ceiling is $110,000.

Write the costs behind the $25,000 rather than using it as an unexplained catchall. Consider purchase closing, lender points and interest, property taxes, insurance, utilities, lawn care, permits, cleanup, staging where applicable, commissions, transfer charges and seller closing costs. Some costs depend on sale price or time. Recalculate them when the model changes.

The repair contingency is for construction uncertainty. It is not permission to ignore incomplete scope. Get property-specific contractor estimates, identify exclusions and determine who is responsible for permits, inspections and change orders. Keep a separate cash reserve for obligations beyond your planned project budget.

3. Stress the exit separately

At a 5% lower sale price, $200,000 becomes $190,000. With the same simplified repair, contingency, other-cost and target-profit assumptions, the maximum purchase price becomes $100,000. At a 10% lower sale price of $180,000, it becomes $90,000.

Those calculations hold other costs fixed only to make the lesson clear. Selling costs and interest can change as price and time change, so replace them with the terms of your actual project. The 5-10% stress is a test of a lower exit, not a

promise that prices cannot fall further. The repair contingency remains a separate line.

Nate's perspective: If my acceptable profit disappears under a reasonable downside, I want a lower entry price or I pass. I do not want to fund a renovation while hoping the market rescues a thin deal.

4. Ask what happens when the schedule moves

Suppose your base plan assumes a five-month hold, but a permit delay and contractor change add two months. Calculate two additional months of interest, taxes, insurance, utilities, lawn care and any other ongoing obligations. Then ask whether the sales season, financing maturity, insurance coverage or buyer demand has changed. A loan extension may have its own conditions and cost; ask the lender rather than assuming one is available.

Do not model a delay merely as extra interest if the scope must also change. Likewise, do not count the same change order in both the original scope and a second contingency charge. Track original budget, approved changes, payments made and funds remaining.

5. Three decisions at the same asking price

Imagine a seller asks $105,000. The base-case ceiling is $110,000, so the price might initially appear acceptable. But the 5%-lower exit ceiling is $100,000 under the simplified assumptions. At $105,000, the same stressed sale would leave $20,000 rather than the $25,000 target, before income taxes; actual price-dependent costs may alter the result.

You can investigate the comparable sales, repair scope and lender quote, then determine whether a lower offer is supported. If the seller will accept $95,000, the deal may merit further work; inspection could still reveal a $15,000 foundation issue that changes the answer. If the seller is firm and the risk-adjusted profit does not meet your requirement, pass. A seller's reason for needing a certain amount does not change the economics, but it deserves a respectful conversation.

6. The contractor conversation

Walk through the property with a written scope and ask the contractor to identify what is included, excluded and uncertain. Request a schedule, payment milestones, proof of appropriate credentials and insurance, and a process for documented changes. Confirm permit and inspection responsibilities for the work and location. Avoid treating a rough verbal estimate as a fixed, complete project bid.

During the project, compare actual spending with each budget category and reconcile invoices against work performed and agreed terms. When a surprise appears, document the reason, price, schedule effect and authorization. Then rerun the deal using the updated forecast. Knowing early that a target has slipped gives you more choices than waiting until the house is on the market.

Your flip decision sheet

1. What finished condition does the ARV assume, and which closed sales support it?

2. Is the repair scope complete enough to obtain reliable bids?

3. What repair contingency and separate cash reserves are available?

4. Are purchase, finance, holding and resale costs included once?

5. What is the target profit before income tax and how much remains at a 5% and 10% lower exit?

6. What happens if the project takes two months longer or requires a major change order?

7. What maximum offer meets the constraints, and what would cause a pass?

Use the deal-analysis course, renovation course and deal tools to test your own assumptions. Verify local requirements and consult appropriate professionals for the property and transaction.

Walk through a project when the facts change

Assume you are evaluating a hypothetical home with a supported finished value of $220,000. Your preliminary scope is $40,000, the separate repair contingency is $8,000, other fixed acquisition, finance, holding and selling costs are $30,000, and your target profit is $25,000 before income tax. Under these simplified assumptions, the base purchase ceiling is $117,000.

Now test a 5% lower exit. At $209,000, the same simplified ceiling is $106,000. At a 10% lower exit of $198,000, it is $95,000. Selling costs that depend on the sale price and financing costs that change with the loan or hold period need to be recalculated; the fixed-cost example is a teaching shortcut. If you need the target profit to survive the 10% lower exit, the $117,000 base ceiling does not provide that protection.

Suppose the seller is willing to discuss $100,000. That does not end the analysis. Your contractor opens the damaged bathroom wall and identifies a $6,000 issue not included in the original scope. If you allocate it against the $8,000 contingency, do not also add it a second time on top of the full contingency. But only $2,000 of the original allowance remains for other construction uncertainty. Ask whether that remaining amount is sufficient and whether the work changes the schedule or required approvals. A contingency that is fully consumed before work starts may need to be replenished in a revised forecast.

Protect your assumptions about the resale

Picture two nearby sales at $215,000 and $225,000. The first has a similar layout but a newer roof; the second has an additional bathroom and a larger lot. A simple average gives $220,000, but it does not automatically establish the value of your finished home. Investigate each difference and ask an experienced local professional which sales are actually comparable. The work budget needs to deliver the condition assumed by the comparison.

If relevant evidence supports only $210,000, use that as the starting value when rebuilding the model. A 5% lower exit from $210,000 is $199,500 and a 10% lower exit is $189,000. Under the same fixed $40,000 scope, $8,000 contingency, $30,000 other costs and $25,000 profit target, the corresponding simplified ceilings are $96,500 and $86,000. The point is not to predict a particular sale; it is to see how much your offer depends on the valuation.

Review the timeline as a sequence of obligations

Create a calendar showing loan maturity, draw requests, permits, trade work, inspections, listing preparation and expected sale. Ask which tasks can happen at the same time and which depend on an earlier approval. A two-week delay at the start may push several later tasks; it may also overlap with work already scheduled. Model the actual carrying costs for the additional period rather than adding a generic penalty.

Review the insurance terms for a vacant or renovated property and ask the lender how extensions work before depending on one. If a lender's extension involves a fee, additional interest or approval, include the actual terms. Keep the cost of an extension distinct from the repair contingency. If the revised project no longer meets your return or liquidity requirements, reassess your alternatives with the professionals responsible for the work and financing.

What I would explain to the seller

'Based on the comparable sales I can support today, the repairs, the cost to carry and sell the house, and the risk that the exit is lower than expected, the price I can justify is below your asking price. I would want to verify the condition and closing details before making a final commitment.'

The seller may disagree, and they may have a better option. A respectful explanation does not require you to claim your estimate is an appraisal or that the seller has no choice. It gives the other party a clear understanding of the basis for your offer while preserving your willingness to pass if the numbers do not work.

Decide whether the upgrade pays for itself

A contractor proposes a $9,000 kitchen upgrade during a flip. The agent thinks it might support another $12,000 of gross resale value. Before approving the work, verify which comps actually support the difference. At a hypothetical 6% incremental selling cost, the added sale price contributes $11,280 before the upgrade, leaving $2,280. If it adds two weeks and $1,500 of carrying costs, the margin narrows to $780. A small pricing miss can erase it. Keep repairs required for safety or the promised scope separate from discretionary upgrades; the first group may not be optional.

Field exercise: The buyer asks for a concession

The facts you have

A flip goes under contract at $220,000. The buyer asks for a $7,000 closing credit after inspection. A second potential buyer informally mentions $216,000, but has not submitted an offer. An extra month would cost $1,800 to carry. Assume identical fixed closing costs for this exercise.

How I would work it

The first buyer’s gross economic proceeds are $213,000 before other costs. A second transaction at $216,000 with one extra month of carry would contribute $214,200 on these simplified assumptions, only $1,200 more. It is not yet a contract, and its timing, financing and inspection terms may differ. Evaluate the written alternatives rather than treating the higher informal figure as guaranteed.

Work the next decision

Run a case where the second transaction takes two extra months. The comparable amount drops to $212,400. What terms or evidence would justify choosing that path anyway?

An offer starts with the evidence you can defend

Think about the first conversation you will have after the rehab. A buyer walks in and compares your property with what they can buy for the same money. They do not care that your contractor charged more than expected or that you paid interest through another month. They are going to compare the layout, condition, location and price with their alternatives. I want to make that same comparison before I buy.

Start with a short list of sales that explain how a typical buyer might see the finished house. Look at closeness, timing, size, condition and material features. I would rather have three sales I can explain than nine numbers that make a good average. If a property is larger or has a bedroom configuration yours cannot offer, put that difference in the notes. If a sale is from another pocket with a different buyer experience, explain why it still belongs or leave it out. Ask the local professional to describe the evidence, not simply affirm the value you gave them.

Keep completed sales and listings separate. A nearby listing tells you what a future buyer might compare; it does not establish that anyone paid that amount. Also distinguish a pending sale's asking price from the verified closed price you may learn later. Record when the comparable information was gathered. A new listing or closed sale can change your view of the exit before you have taken title, so set a point to review it again before a commitment. Do not give yourself

credit for a feature that has not made it into the verified scope.

If you can defend a plausible range of $205,000 to $218,000, avoid grabbing $218,000 just because it lets you meet the asking price. Select a supportable planning figure and record why. Then run the downside against that planning figure. An investment decision that works at the strongest comp and nowhere else requires the strongest comp to become your outcome. I do not want to finance a project that needs that kind of help.

Tie the scope to the price, then challenge the scope

Picture two similar homes. One comp sold after a conventional update with functional windows, a clean kitchen and a documented new roof. The proposed house needs a roof, but the preliminary budget includes only cosmetic updates because a seller described the leak as “nothing serious.” There is a mismatch between the comparison and the scope. Get the appropriate inspection and priced work before treating the comp as a finished-value reference. A spreadsheet cannot make two different conditions comparable.

I put work into three buckets. First, what has to be done to make the house safe, functional and ready for its intended use? Second, what work is required to make the finished product comparable with the sales I am relying on? Third, what am I considering because it could improve the outcome but is not supported yet? The last group needs a decision, not an automatic yes. If a buyer is likely to appreciate a better layout more than another decorative change, get that feedback while you can still change the scope without paying for rework.

Ask who will verify each disputed condition. “Contractor thinks” is not the same as a qualified report on a material

defect. “Permit should be fine” is not confirmation that a specific change is permitted. Check the actual proposed work with the appropriate authorities and professionals. Put the investigation date next to the contractual date by which you need the result. If you cannot verify a major assumption in time, you need to understand your options under the actual agreement rather than assume you can sort it out after purchase.

Build a price from the back: a full numerical walkthrough

Suppose a hypothetical finished sale is underwritten at $225,000. You project $38,000 of defined work, $7,000 of separate contingency, $17,000 of fixed acquisition and carrying costs, variable selling expenses equal to 7% of the realized sale price, and a $27,000 profit target before income taxes. The 7% is an assumption for this exercise; it is not a statement about standard commissions or costs. Use negotiated terms and documented estimates for a real property.

For this exercise the seller purchase ceiling is sale price less variable selling expenses, fixed costs, the scope, contingency and target. At the planning price of $225,000, variable selling expenses are $15,750. The ceiling is $120,250: $225,000 less $15,750, $17,000, $38,000, $7,000 and $27,000. The first time you calculate that number, check whether your carry already includes interest, fees, taxes, utilities, insurance, or any other amount you have put on a different line. I want the same dollar counted once, in the right category.

At a 5% lower exit the sale price is $213,750. Selling expense at 7% is $14,962.50, and the ceiling is $109,787.50. At a 10% lower exit the sale price is $202,500; selling expense is $14,175, and the ceiling is $99,325. Your resale stress

changes the estimated selling cost in this example, but it does not remove the repair contingency or other costs. If a higher purchase price changes debt, fees, points or carrying costs in your actual model, recalculate those as well. The simplified ceiling only works because we explicitly held the other inputs fixed.

Now assume the seller would take $106,000. At the 5% lower sale your projected profit before income tax is $30,787.50. At the 10% lower sale it is $20,325. The deal still shows a positive number in the deeper downside but misses the target by $6,675. If you said at the beginning you would require the target at the 10% lower exit, be honest about that miss. A positive outcome under an assumed scenario and a deal that clears your benchmark are different statements. If your policy would allow a lower target, explain why before changing it. Do not quietly move the target after falling in love with the property.

Use the same habit if the seller offers a credit or changes timing. A credit that can actually be used under the documents may change cash required, the project cost or both. A shorter closing can raise costs or reduce your time to investigate. Ask the people responsible for financing and closing how the terms will be reflected. Write down the net change, not just the amount announced on the phone.

Exercise: what if the scope and sale both move?

Using the same model, suppose a qualified estimate increases known work by $4,000 and you deliberately keep the original $7,000 contingency for unrelated uncertainties. Carry also rises $1,800. What is the revised purchase ceiling in the 10% lower exit case? It is $93,525: $99,325 minus $4,000 and $1,800. At the previously discussed $106,000 purchase, modeled profit would be $14,525 before income tax, assuming nothing else changes. That is a materially different risk and return than the base model. The result is not permission to neglect the new work; it tells you what a revised offer would have to support.

Now assume the contractor's $4,000 estimate covers something already included in your original $38,000 scope. You should not add it again. Read both estimates and decide whether the change is a new cost, a substitution, or merely the same work described differently. With only the $1,800 increase in carry, the revised 10% downside ceiling would instead be $97,525. An argument about which quote is right is hard to resolve if both people are working from an undocumented scope. This is why I prefer written detail over verbal totals.

Use a schedule that lets you see a delay coming

A schedule should show who does the work, what must happen first, how much cash is due and what “complete” actually means. Start by identifying the work that can hold up other tasks. If a roof repair has to stop a leak before interior finishes can proceed, it needs a reliable date before you schedule paint. If you need a review or permit, ask the appropriate authority and contractor what is required and when you can realistically have it. Do not assume your schedule is proof of approval.

Create milestones that you can inspect. Instead of writing “bathroom, week four,” describe what must have been installed, checked or corrected before the next trade can start and the corresponding payment can be made under the agreement. Keep the date, expected cost, person responsible and evidence together. The goal is to notice a schedule slip when you still have options. Finding out at the end of the month that a missing part will add three more weeks is a bad way to discover how closely your forecast depended on the date.

Track time in two currencies: direct cash and choice. An extra month of interest, taxes, utilities, insurance and other carrying expenses has a measurable cost. It may also leave fewer options if the loan approaches maturity or a buyer's financing is uncertain. A project model can show another $1,700 of carrying costs without answering whether you have an agreed extension or enough liquidity to use it. Verify the actual loan documents and work through alternatives early.

A realistic surprise, step by step

Suppose a hypothetical project is scheduled to list on September 1. A cabinet supplier says replacement parts will not arrive until September 22. The contractor believes work can finish a week after the parts arrive. If you were planning to complete pictures and list immediately after construction, your planned date has slipped about four weeks. Ask what work can proceed without the parts, when the installer is available, and whether the agent can prepare materials or schedule photos without representing the property as ready. Use an updated list date based on those facts, not just the supplier's estimate.

If the four weeks cost an additional $1,650 to carry, put that in the model. Consider whether the date moves the entire closing schedule and whether a realistic alternative exists. A temporary substitute that does not match the approved scope may cost more than it saves, especially if it causes another change later. Talk with the contractor about your options, obtain priced terms, and compare them with the actual cost and risk of waiting. Never assume an alternative can skip required work or a review.

Suppose an appropriate, documented substitute costs $850 more and shortens the delay by three weeks. At an illustrative $412.50 of carry per week, it could save $1,237.50 of carry. The simple difference is $387.50 before other effects. Ask whether the substitute changes the buyer's expected condition, warranty or remaining schedule. A narrow numerical advantage is not a reason to authorize a change if the facts make the outcome less certain. It is a reason to ask a better question of the people who can verify it.

Keep your contractor conversations useful when the budget gets tight

I like questions that make the next decision smaller. “How much will it cost?” is necessary, but “What exact work is included, which part is still uncertain, and what happens if we wait for a second opinion?” usually produces a better answer. If the work is urgent to make the property safe, address that with qualified help before comparing discretionary options. For other changes, ask for a written scope, cost, deadline, and impact on the next trade. Look at your actual contract for how changes and payments are handled.

A progress photo is useful evidence of something visible. It may not prove the whole milestone is complete. Compare the completed work with the written scope, approved changes and any qualified inspections applicable to it. Ask who is responsible for the final verification. If your deal depends on drawing loan funds for a completed milestone, confirm which proof the lender needs and when it can inspect. A contractor and a lender can both be acting reasonably while using different dates for when they expect payment and disbursement.

Think through the first change conversation before you need it: “What has changed from the original assumptions? Is it safety-related, required to deliver the agreed scope, or an option? What can we verify now? What other work does it move? When do you need a decision?” Write down the response. I don't want to argue in circles because one person remembers a phone call differently. I want to know the cost, what evidence supports it and what it does to the exit.

Watch the cash balance between milestones

A hypothetical project has $31,000 available for work after closing, separately from the reserve floor you intend to protect. The contractor needs $9,000 in week one and $13,000 when the next phase starts. Taxes, interest and other obligations in that period are $2,000. After those outlays you have $7,000 available. You expect a $12,000 renovation draw, but it will arrive after a lender review. Before the draw date, another $9,000 payment is due. There is a $2,000 timing gap. On the original budget the draw would eventually arrive, yet on the actual calendar you cannot pay all of the bills without using money you intended to protect.

The best time to solve this is before buying. Review the draw milestones, required paperwork and expected processing times with the lender. Compare them with the payment terms you actually negotiated. Ask whether a changed sequence can be documented without interrupting the work. If you need additional funding, verify the source, terms and cost before relying on it. Calling the lender after the contractor is ready to walk is a late way to discover that the lender and contractor are looking at different cash calendars.

A draw that repays a verified expense is a funding source, not a second sale or a project profit. Keep both sides of the cash movement visible. A delay can matter even when every expense will be paid as projected later. My reserve is there for actual obligations and surprises, but I do not treat using it as part of the planned budget just because the budget otherwise fails on paper.

Exercise: separate a budget overrun from a timing gap

Assume the $12,000 draw arrives two weeks later, in full, with no incremental interest or costs solely for this exercise. What is the direct change to budgeted expenses? None in the simplified facts. What was the cash shortfall before receipt? $2,000. If the delay adds $900 of verified carry, the cost forecast increases by $900. If that expense is due before the draw, the timing shortfall could also increase to $2,900. In a live model map each payment to its actual date and recalculate the minimum balance before concluding either number is correct.

The listing decision is a business decision

When the work is close to complete, ask your agent to refresh the comparison against the actual finished property. The original range was a purchase assumption; it is not a promise the market made. Look at competing homes, relevant closed sales, condition and terms. If an agent recommends pricing lower, ask what the evidence says and what would justify holding out. Then compare expected proceeds and timing at plausible price points rather than confusing an asking strategy with realized value.

Suppose you are comparing an offer at $208,000 expected to close sooner with another written offer at $214,000 that includes a $3,000 credit and would carry another month of $1,600. If both have otherwise identical fixed closing expenses in this teaching example, the second option contributes $209,400 after that credit and extra carry, only $1,400 more than the first. If your actual selling expenses are price-sensitive, update them as well. Next compare contingency, financing, likelihood of closing and the cash you

have available to wait. A difference of $1,400 may justify waiting in one situation and not another. I care more that I can explain the choice than that I have the higher headline contract.

Review whatever closing statement or settlement estimate applies with the people handling the transaction. Check the debt payoff date, credits, closing charges and other amounts against the model. A refund, deposit return or draw may have already appeared in your ledger; make sure you don't use it twice when reconciling proceeds. Compare the actual project with the original underwriting and identify the earliest point where you could have known about a meaningful deviation.

The decision record I want at each stage

Before the offer, record the supported value range, the scope necessary to deliver that condition, fixed and variable costs, financing, liquidity, base case and stressed ceilings. State which ceiling actually governs and why. Write the evidence still needed and who will get it. A conditional offer does not remove the need to understand exactly what the agreement says, and no verbal promise should substitute for the terms you are relying on.

Before work starts, record the agreed scope, responsible people, milestone dates, expected cost, financing draw timing, reserve and decision process for changes. Before listing, record completed work, remaining obligations, confirmed condition, current evidence on price, the updated sale forecast and how much time you can afford. After closing, write down actual costs, the net proceeds, cash invested, the realized result before taxes and what your estimates missed.

If the project performed better than expected, ask which part came from buying well or executing well and which part came from circumstances you could not count on. A favorable sale does not prove that it was smart to run out of reserve. If you missed the target, identify the earliest assumption that needed more evidence and change your next decision process. The money earned on one deal matters. So does the habit you carry into the next one.

Final practice: explain why you would pass

An asking price is $104,000. Your fixed project costs excluding purchase, including defined work and separate contingency, total $69,000. Your supported finished value is $215,000, modeled variable selling costs are 6% of realized sale price, and your target profit is $25,000. Your policy for this exercise is to meet that target at a 10% lower sale. Compute the ceiling and decide whether to offer the asking price.

The stressed exit is $193,500. At 6%, modeled variable selling costs are $11,610, leaving $181,890 before the fixed project costs and purchase. After deducting $69,000 and $25,000, the ceiling is $87,890. At $104,000, the stressed projected profit is $8,890, below the target by $16,110. Do not pay the asking price under the stated rule just because it still shows profit on paper. A lower offer might be considered if the supportable numbers and contract terms line up. Verify the fixed and variable costs, the value evidence and the cash schedule before relying on any number.

Write three sentences to explain the decision: one describing the actual property assumptions; one stating which number controls the offer; one identifying what could legitimately change that conclusion. If you can only explain the deal by

switching from stressed to base-case numbers after the seller says no, you have your answer. There will be another property. You still need the cash and time to be able to evaluate it when it comes along.

Optional case: When a promising deal stops working

At the $105,000 ask, the same house has a supported $190,000 resale assumption after work. Known repairs start at $30,000. Add $22,000 of other costs, including a separate repair contingency, and a $22,000 target for pre-tax profit. The preliminary base offer ceiling is $116,000. An inspection adds $8,000 of work outside that original scope. The updated ceiling is $108,000 at the base exit, $98,500 at a 5% lower exit ($180,500), and $89,000 at a 10% lower exit ($171,000), holding other costs fixed for the exercise.

At $105,000 the base screen clears, but both lower resale scenarios miss my profit target. I would verify the revised scope and the comps, recalculate costs that move with price or time, and negotiate only to a ceiling I can defend. Otherwise I pass. I would not spend the same contingency twice or treat a lower resale assumption as a substitute for it.

Where I’d draw the line

I’d draw the line at the offer the downside can support. If the comps and timing make a 10% lower exit the right test, I negotiate from the $89,000 ceiling in this example. I don’t use the $108,000 base ceiling to talk myself into the ask. On your next flip, write your downside ceiling next to your offer before you call the seller.

See how the full deal played out in the optional case in Is This Really a Good Real Estate Deal?.