



## TYPES OF BIDDING



The types of bidding used at tax lien auctions are specified by the taxing jurisdiction. No matter the type of bid, the jurisdiction will set a minimum bid that will cover the delinquent property taxes, penalties, costs and fees.

There are four types of bidding used. These are highest bid, buyer's bid, interest rate bid and property interest bid.

### 1. Highest Bid

- ↳ The bidder who makes the highest bid over the amount due for the tax lien is the winning bidder. Any amount you pay for the tax lien beyond the amount due is put into an account that earns interest over time.
  - ∞ This excess amount is called the bid premium. If the property owner redeems the tax lien, this money and the interest it has received are transferred to you. This is in addition to the tax lien face amount and the interest that is paid back by the property owner.
  - ∞ There is one caveat on the bid premium being transferred to you. If the tax lien is not redeemed by the property owner, and you are issued a tax deed, the property owner may have the right to these funds.

*Example:* Three bidders are bidding on a tax lien with a face value of \$3,700.

Bidder 1 bids \$4,100, Bidder 2 bids \$4,150 and Bidder 3 bids \$4,200.

Bidder 3 wins the bid and receives the tax lien. If the property owner redeems the tax lien, bidder 3 will receive \$3,700 plus interest on that amount and will receive another \$500 plus interest back, which is the premium bid.

Winning Bid	\$4,200
Tax Lien Amount Returned	<u>\$3,700</u>
Bid Premium	\$ 500



## 2. Buyer's Bid

- ➔ The buyer's bid is similar to the highest bid. You will bid a dollar amount for the tax lien. However, the amount of your bid that is in excess of the amount due on the tax lien will not be returned to you if the property owner redeems the tax lien. The more you pay for the tax lien, the lower your investment yield will be.

*Example:* Three bidders are bidding on a tax lien with a face value of \$3,700.

Bidder 1 bids \$4,100, Bidder 2 bids \$4,150 and Bidder 3 bids \$4,200.

Bidder 3 wins the bid and receives the tax lien. If the property owner redeems the tax lien, bidder 3 will receive \$3,700 back plus interest on that amount. The \$500 becomes part of the cost of doing business.

Winning Bid	\$4,200
Tax Lien Amount	\$3,700
Amount Returned	<u>\$3,700</u>
Cost of Doing Business	\$ 500

## 3. Interest Rate Bid

- ➔ Bidders bid on the minimum interest rate that is acceptable for them to receive. Bidders do not bid a tax lien amount. The winning bidder will have to pay the delinquent taxes and penalties in full.
  - ∞ The winning bidder will receive a tax lien for that amount. The interest received is the bid. A bid cannot be an interest rate that is higher than what the taxing authority can legally charge the property owner.

*Example:* Two bidders are bidding on a tax lien with a face value of \$3,000. Bid begins at 18% per six-month interval.

Bidder 1 bids down to 7% for the six-month interval, or 14% annually. Bidder 2 bids down to 6.5% for the six-month interval, or 13% annually.

Bidder 2 wins the bid, pays \$3,000 and receives the tax lien. If the property owner redeems the tax lien after 18 months, Bidder 2 will receive \$3,000 plus \$195 in interest for three six-month intervals.



Tax Lien	\$3,000
Interest Rate	6.5%
Six-Month Intervals	3
Interest	\$ 585
Yield	13%

#### 4. Property Interest Bid

- ↳ Bidders bid for an interest in the property. The bidder who is willing to take the smallest portion of undivided interest in the property will win the tax lien. The idea is to protect the property owner. If the property owner does not redeem the tax lien, you can foreclose on your interest in the property.
- ↳ If you have a 90 percent interest in the property you obviously have more security for your tax lien than if you had a 60 percent interest in the property. The general rule of thumb is to have at least a 50 percent interest in the property.

*Example:* Two bidders are bidding on a tax lien with a face value of \$5,000. Either bidder will have to pay the \$5,000 tax lien amount. The tax lien pays 14% annual interest.

Bidder 1 will not take less than an 85% interest in the property. Bidder 2 will take an 80% interest in the property.

Bidder 2 wins the bid. When the property owner redeems the tax lien, the bidder will receive the \$5,000 plus 14% annual interest.

Tax Lien	\$5,000
Interest Rate	<u>x 14%</u>
Interest (one year)	\$ 700

However, if the property owner does not redeem the tax lien, the bidder will have to foreclose on the property and then have an 80% undivided interest in the property. The property owner will retain a 20% undivided interest in the property.

Investor Ownership Interest	80%
Property Owner Interest	20%
Property Value	\$100,000
Investor Value	\$ 80,000

Either redemption, the bidder will come out ahead.