

# Workshops for Modern Real Estate

## General Course Outline

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# WORKSHOPS FOR MODERN REAL ESTATE

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## Session Descriptions

### SESSION ONE (Text Chapters 1, 2, 9, 10)

Characteristics of Real Estate and Personal Property  
Agency Relationships  
Employment and Independent Contractor Agreements  
Real Estate Brokerage and Marketing Regulations

### SESSION TWO (Text Chapters 11 and 12)

Listing Agreements and Buyer Representation  
General Law of Contracts  
Purchase Agreements between Buyer and Seller

### SESSION THREE (Text Chapters 4, 5, 7, 8, 13, 18)

Transfer of Title – Voluntary and Involuntary – Title Insurance  
Estates in Land  
Forms of Property Ownership  
Leasehold Interests  
Easements and Encumbrances  
Real Estate Taxes and Other Liens

### SESSION FOUR (Text Chapters 14, 15, 17)

Financing Principles  
Financing Practices  
Mortgage Foreclosure and Redemption  
Government Oversight – TIL, RESPA, FIRTPA  
IRS Regulations  
Closing the Real Estate Transaction

### SESSION FIVE (Text Chapters 16, 19, 20, 21)

Real Estate Appraisal  
Property Management  
Control of Land Use – Public and Private  
Environmental Issues

### SESSION SIX (Text Chapters 3, 6, 22)

Fair Housing and Ethical Practices  
Equal Credit Opportunity (Review Chapter 15, pages 281-282)  
Real Estate Investment – Tax Benefits and Other Matters  
Property Descriptions and Methods of Measurement  
Real Estate Calculations  
Math Questions – Text pages 479-493, Practice Questions (last pages of book)

# SESSION ONE

## GENERAL PROPERTY CONCEPTS

- I. There are two (2) categories of property:
- A. Personal Property, consisting of things that are moveable and not affixed to the property (chattel OR personalty).  
Examples: stand-alone TV, a cow, a toothbrush, a car, etc.
  - B. Real Property (Realty) consists not only of the land, but also of the things affixed to it, and of the rights in and to the land. (Land, real estate, real property)
    - 1. Examples: six (6) acres of land, the house built on that land, the mineral rights to that land, trees growing on that land, other subsurface rights, etc.
    - 2. Fixture - something that was once personal property, but was permanently affixed to the land or building, and now is considered real property.  
Examples: an apple tree, a bathtub, etc.
    - 3. Trade fixture - an article installed by a tenant under the terms of a commercial lease, which can be removed before the expiration of the lease.  
Examples: Gasoline storage tanks, supermarket shelving, etc.
    - 4. Legal tests of a fixture:
      - a) Intention.
      - b) The method of annexation.
      - c) The adaptation to real estate.
      - d) The existence of an agreement.
- II. When a person owns property, essentially what they own is the legal "bundle of rights" affecting that property. The rights in the "bundle" would include, for instance, the right to possess the property, the right to lease the property, water rights, air rights, the right to control that property, etc.
- A. Property may be owned by one person (ownership in severalty). Examples: an individual, a corporation, etc.
  - B. Or, more than one person (concurrent ownership). Examples: a partnership, husband and wife, a group of non-related persons. (Concurrent ownership may be held in the manner of joint tenancy, tenancy in common, tenancy by the entirety, etc.)
- III. Characteristics of Real Estate
- A. Economic Characteristics:
    - 1. Scarcity - can be limited supply in a particular location or of a particular quality.
    - 2. Improvements - buildings on the land can affect the value and use of the surrounding parcels of land, as well as the improved parcel.
    - 3. Permanence of investment - buildings represents a large, fixed investment.
    - 4. Area preference (situs) - people chose one area over others.
  - B. Physical Characteristics:
    - 1. Immobile - the location of a particular parcel of land is fixed, and can never be changed.
    - 2. Indestructible - the fact that land can endure any combination of forces over time, tends to stabilize investments in land.
    - 3. Land is unique - all parcels of land differ, at least geographically (non-homogeneity).

## LAWS OF AGENCY

- I. An Agent is a person representing a principal in dealings with third persons. The relationship of the agent and principal is called an agency. Subagents are authorized by the principal to assist the agent in carrying out the purpose of the agency.
- A. Principal (client) - hires the agent and gives the agent authority.
1. May be a person, or a form of business entity.
  2. Usually is the seller in real estate, but may also be a buyer, or other person.
- B. Agent - accepts the Principal's hiring and authority.
1. After accepting the authority, the agent owes agency duties to the principal and is owed only a business duty in return.
  2. Agents must be licensed to practice real estate.
- C. Customer - a third person who is not a party to the agency. The customer is the person that the agent has been hired to find (usually the buyer), and owes/is owed only a business duty.
- D. The agency relationship is created by a contract.
1. Can be implied, as well as oral or written. NOTE: Notwithstanding this rule, some states require service agreements to be in writing and signed.
  2. To create the fiduciary relationship, agency agreements must satisfy all of the elements required of other contracts.

### CLIENT

**Agent works “for” Client**  
**Loyalty (good faith)**  
**Confidentiality**  
**Disclosure**  
**Obedience**  
**Care, skill and diligence**  
**Advice**  
**Advocacy**  
**Accountability**

### CUSTOMER

**Agent works “with” customer**  
**Fairness**  
**Honesty**  
**Disclosure of facts/Property Condition**  
**Good Service**  
**Reasonable care skill and diligence**  
**Consultation**  
**No Advocacy**

- E. Agents' fiduciary responsibilities (See Chart Above) to principal (COALD) under the Law of Agency:
1. Care - There is no guarantee that the agent will be able to perform, but the agent must make maximum effort to fulfill agency obligations.
  2. Obedience - The agent must operate within the legal scope of his/her authority (ex. listing prices).
  3. Accounting - The agent must account for the funds and other property placed in his/her care.
    - a) Must keep accurate records. State law determines for how long.
    - b) No commingling (includes waiting too long to deposit in trust account).
    - c) Trust (escrow) account must be maintained to hold funds entrusted to the broker.
  4. Loyalty - The principal's best interest must come before the agents'. Must never act as an "agent and an undisclosed principal in the same transaction."
  5. Disclosure - The agent must keep the principal aware of any material information that could impact on the sale/purchase of the property. There is a duty on the part of the agent to discover certain important information.

F. Types of Agents- The amount of authority an agent is given by the agency contract determines the type of agent (s)he will become.

1. Special Agent - has been given the least amount of authority. (S)he can represent the principal in only one specific transaction or business activity. (Ex. a broker given the authority in a listing to find a "ready, willing and able buyer".)
2. General Agent - given a "general power of attorney" to represent the principal in a range of transactions or activities (ex. to run a business, or manage property for the client).
3. Universal Agent - given a "Universal" power of attorney.

G. Client Relationship Categories

1. Seller Agency & Buyer Agency – In the past, most agency relationships in real estate involve the agent (Principal Broker) working for the seller. Today it is very common for buyers to hire their own agents. The Principal Broker is the agent of the seller or buyer. If a firm ONLY represents Sellers or ONLY represents Buyers, the firm is known as a “Exclusive Agency.”
2. Dual Agency - When an agent is representing both sides in the same transaction.
  - a) At common law, dual agency is permissible only if disclosure is made to both principals and both principals consent.
  - b) Undisclosed dual agency is never allowed. Often undisclosed dual agency is inadvertently created when an agent for a seller implies that (s)he is working for the buyer; less often for the seller. This is known as “implied agency.”
3. Sub Agency – Licensee’s firm represents another firm and such other firm’s client. In such case, licensee’s firm is an agent of the other firm and a subagent of Such other firm’s client.
4. Designated Agency – Also called “appointed agency” where a particular agent or particular agents in a firm is/are designated (or appointed) as the exclusive agent for the client. Rules vary from state to state. Typically agents from the same firm can be appointed to represent separately both sides of the transaction, with safeguards to ensure confidentiality. Usually liability of the firm is not affected. This form of client representation was not available at common law and exists only where a state’s statutes authorize it.

H. Agents responsibilities to third parties- non-client a/k/a customer (still most frequently the buyer).

1. Honest and fair dealing.
2. Duty to disclose material defects which affect the property if known by the licensee.

I. Non-Agency Relationships – Some states provide for “another relationship” to be established between the brokerage firm and the customer (non-client). The services being provided usually must be set forth in writing. Examples include so-called Transaction Brokerage or Facilitator.

## II. Miscellaneous Agency Issues

### A. Compensation in General

1. Must be specified in the listing agreement.
2. Can be a percentage of the sales price, with the broker receiving the same percentage if the price increases or decreases or, a flat dollar amount - as long as the listing defines some form of "specific consideration".
3. "Net listings" and frowned-up and are outright illegal in many states.
4. Commissions are always negotiable between the client and the agent. Brokers can never conspire to "fix prices."
5. The agent may be entitled to a commission even if the transaction is not successful, however, (s)he may have to sue the client to receive payment. Only the listing broker has standing to sue the client.
6. When suing a client for a commission, the broker must prove to the court that (s)he:
  - a) Was licensed at the time of the transaction;
  - b) Was hired with a (written) contract by the principal; and
  - c) Found a "ready, willing, and able" buyer.
7. In a commission dispute between two (2) or more brokers, the court (not the Real Estate Commission) will award the commission to whichever broker can prove that (s)he was the "efficient and procuring cause" of the sale. This standard applies to open listings. The standard may similarly apply when there is a dispute between the Seller and his/her broker under an Exclusive Agency type listing.

### B. Salesperson's Compensation

1. Is usually a share of the commission; and is only paid to the salesperson through his/her broker
2. Must be specified in an agreement between the broker and the salesperson.

### C. The Nature of the Brokerage Business

1. Brokers may reject any agency contracts so long as not for illegal purpose.
2. Salespersons who are licensed under a broker are responsible to that broker. All of salespersons' activities must be performed in the name of the employing broker.
3. Principal brokers are directly AND vicariously responsible for supervising all of his/her sales associates' real estate business activities. The same would be true of a branch office broker-manager with respect to licensees in the branch.
4. Rule applies whether the salesperson is associated with the broker as an employee or as an independent contractor.
  - a) Sales associates are also liable for their own acts.
  - b) IRS defines as one of the qualifications regarding the difference between "employee" and "independent contractor" a determination of how much control the broker maintains over the business activities of the salesperson (no benefits may be provided to an "independent contractor").
  - c) Basic IRS guidelines include written agreement, licensure, and 90% rule
  - d) Independent contractor contracts with a firm are for federal income tax purposes. The agent will get a 1099MISC at the end of the year.

# SESSION TWO

## LISTING AGREEMENTS

A listing agreement is an agency contract between the Principal and Agent. SELLER-AGENCY is a listing (service) agreement (agency contract) with a SELLER (owner) of real estate (as principal) and a real estate broker or brokerage firm (as agent) by which the SELLER hires the brokerage firm to find a **ready, willing and able buyer**, and agrees to pay the brokerage firm a commission when such a buyer is found. BUYER AGENCY is an service agreement (agency contract) between the BUYER of real estate (as principal) and a real estate broker or brokerage firm (as agent) by which the BUYER hires the broker to find a **ready, willing and able seller**, and agrees to pay the brokerage firm a commission when such seller is found.

### I. Creates a special agency relationship.

- A. The broker is authorized either to represent the Owner and the Owner's property to third parties known as un-represented buyers (customers) OR to represent the Buyer in the search for third party defined as an unrepresented Seller (customer).
- B. As a special agent (See Class # 1 Outline) under the agency contract, the broker and brokerage firm is not authorized to bind the principal to a sale.
- C. Only licensed real estate brokers designated as principal broker for a registered brokerage firm can be hired by the seller, buyer, lessee, and lessor to perform brokerage services.
- D. Under a brokerage (firm) practicing designated agency the appointed licensee, as a designated (or appointed) agent, is the Agent of the client (principal). The Principal Broker and brokerage firm is not a fiduciary to the client. NOTE:

### II. Some states require service agreements to be in writing and signed by a licensee of the firm on behalf of the brokerage firm, and also signed by the owner(s) or buyer(s). Option Listings - Broker has right to purchase may be included in agreement. Following are the basic types of service (listing) agreements:

- A. Exclusive-Right-To-Sell (Seller-Agency) OR Exclusive-Right-To-Buy (Buyer-Agency)
  1. One broker is hired to be the sole agent for the seller (Seller-Agency) OR One broker is hired to be the sole agent for the buyer (Buyer-Agency)
  2. The seller gives up the right to sell the property herself without paying a commission to the broker (Seller-Agency) OR the buyer gives up the right to purchase the property herself without paying a commission to the broker (Buyer-Agency)
  3. Gives the broker the most protection.
- B. Exclusive-Agency Listing
  1. One broker is authorized to act as the exclusive agent of the seller (Seller-Agency) OR one broker is authorized to act as the exclusive agent of the buyer. (Buyer-Agency)
  2. The seller keeps the right to sell the property herself and not have to pay the broker a commission (Seller-Agency) OR the buyer keeps the right to buy the property herself and not have to pay the broker a commission (Buyer-Agency)
- C. Open (Non-Exclusive) (Simple) Listing
  1. The seller may give an open listing to any number of brokers (so there can be one client and many agents) (Seller-Agency) OR the buyer may give an open listing to any number of brokers (so there can be one client and many agents) (Buyer-Agency)
  2. The seller keeps the right to sell the property himself and not have to pay a commission. (Seller-Agency) OR the buyer keeps the right to buy the property

- himself and not have to pay a commission (Buyer-Agency)
3. Once a buyer is found, all of the other listings automatically terminate (Seller-Agency)  
OR once a seller is found, all of the other listings automatically terminate (Buyer-Agency)
- D. The Customer and Agency (Brokerage Firm) may determine services to be rendered with the possibility of not establishing an “Agency Relationship” between Agency and Customer. An example of such services may include “ministerial acts” or similar so-called “non agency” services permitted (and often specifically outlined) by statute in a particular state.
- III. Multiple Listing Service - a marketing organization whose brokerage firm members agree to make their own exclusive listings available to other members who then share commissions on cooperating sales.
- A. Usually the original listing broker is responsible for showing the property, getting contract approval, holding the deposit, etc. This can vary by agreement and custom.
  - B. The listing brokerage firm is paid the commission by the seller and then the listing brokerage firm "splits" it with the buyer's brokerage firm OR cooperating brokerage firm as agreed.
  - C. The listing Principal Broker and his or her Brokerage Firm are usually the agent under the property listing (but this changes in firm's allowed to practice designated agency).
  - D. If the Brokerage Firm working with the buyer is not the seller's Brokerage Firm, the licensees of that other Firm may be the sub-agent of the Seller.
- IV. Splitting Commissions (Co-broking)
- A. Commission splits can be given only to real estate licensees.
    1. Within a Brokerage Firm, the principal broker may split commissions with his/her licensees.
    2. Outside a Brokerage Firm, the principal broker can split commissions only with other Brokerage Firms in-state or out-of-state. A licensee never receives commission splits or bonuses from anyone other than his/her principal broker.
  - B. Compare referrals (see Outline Part XII below)
- V. Net Listings - Seller requires a certain amount of money to be netted from the sale of his property. If the broker can sell the property for more than the amount the seller wants to net, than she can keep the difference as her commission. Net listings are illegal in both Vermont and New H Hampshire.
- VI. Listings terminate for the following reasons:
- A. Performance.
  - B. Lapse of the time period specified in the listing.
  - C. Breach or cancellation by one of the parties.
  - D. Transfer of the title to the property by operation of law (ex. bankruptcy).
  - E. Mutual consent.
  - F. Death or insanity of either party.
  - G. Destruction of the property.
  - H. Change in property use by outside forces (zoning, eminent domain are examples)
  - I. Suspension or Revocation of the License of the Broker.
- VII. As a personal services contract, a listing is not assignable.

- VIII. Look to state law to determine whether service agreements are required to include a specific expiration date and whether or not such agreements may contain provisions for automatic extension and/or renewal. For example: Is it permissible to include a provision automatically extending the term of a listing when the property goes under contract for sale during any time when the listing is still effective?
- IX. Listing the Property - The property should be listed for a price that is competitive and realistic to the marketplace.
- A. Licensees may prepare a CMA (competitive market analysis) to help establish a realistic selling or purchase price. CMA's are NOT appraisals. Only a licensed or certified appraiser may perform an appraisal. (Market Value and Market Price)
  - B. The seller-client has the privilege of setting the selling price and the buyer-client has the privilege of setting the purchase price.
- X. Required Information on Service Agreements
- A. Description of the type of agreement
  - B. Description of the property
  - C. Price (asking price), terms, and conditions under which the brokerage firm may market the property (seller agreements)
  - D. Description of services to be provided and any limitations on service
  - E. Any required disclosures such as conflicts resolution, sharing of commissions with other firms, nature of agency relationship, limitations and qualifications on representation
  - F. Compensation and who will pay and when
    - 1. Open for negotiation between client and firm
    - 2. Commissions due after agreement expires – “broker protection clause” (optional)
  - G. Signatures of all parties
- XI. If a broker takes a service agreement which gives the broker the authority to represent a buyer in the purchase of real property, some state statutes specifically require disclosure of this relationship at the first instance of contacting the seller or seller's agent.
- XII. Referrals are NOT service agreements and do not create an agency relationship
- A. Active licensure is required, but not necessarily in this state
  - B. No requirement that agreements be in writing and other terms usually not regulated
  - C. Usually limited to paying for a name; active participation in the transaction is prohibited unless properly licensed in the state where the property is located

## CONTRACTS

- I. A contract is a voluntary agreement between legally competent parties to perform or refrain from performing some legal act. Contracts must be supported by consideration.
- A. Contract Law
- 1. Contracts may be oral, written, or even implied by the actions or conduct of the parties.
  - 2. Express Contract - where the parties specify the important terms and conditions of the contract (example: an option agreement).
  - 3. Implied Contract – where the conduct of parties are viewed by law to constitute agreement to certain terms

## B. Types of Contracts

1. Bilateral contracts - bind all parties and are enforceable against all parties (example: a purchase and sales agreement).
2. Unilateral contracts - are binding on and enforceable against only one party (example: an open listing agreement).
3. Executed contracts are those that have been fully performed.
4. Executory contracts require some performance by one or more parties before they are completed.
5. Validity of Contracts
  - a) Valid - complies with the essential elements of a valid contract.
  - b) Void - has no legal effect (example: a contract for an illegal purpose).
  - c) Voidable - may be disaffirmed or voided by one party (example: a contract entered into by an incompetent person).
  - d) Unenforceable - no party may sue for performance (example: an oral purchase and sales agreement).

## C. Elements essential to a valid Contract

1. Legally competent parties
  - a) Must have the mental capacity necessary to understand contractual rights and obligations (legal capacity/contractual ability).
    - (1) Of legal age
    - (2) Under no mental impairment
    - (3) Not under the influence of drugs (including alcohol)
    - (4) Not under duress or coercion.
  - b) Contracts entered into between a competent person and an incompetent are voidable on behalf of the incompetent. Example: Minors.
  - c) Corporations get contractual ability through approval by a quorum of the corporate board of directors. Without quorum approval, any corporate contracts would be **ultra vires**.
2. The parties must have a "meeting of the minds" (mutual assent, offer + acceptance) - the parties must understand and agree to the terms of the contract.
  - a) Offerors must:
    - (1) Intend to make an offer
    - (2) Actually communicate the offer to the offeree
    - (3) Specifically describe the property and the price in the offer
  - b) Before acceptance, offers are terminated by:
    - (1) The death of either party
    - (2) Rejection of the offer
    - (3) Revocation of the offer
    - (4) Counter-offer (a rejection and new offer by original offeree)
    - (5) Lapse of a "reasonable time"
  - c) Acceptance of an offer must be by overt behavior or words.
3. There must be "Legality of Object" (the purpose of the contract must not be illegal or against public policy).
4. Consideration - something of value must "flow from both sides" of the contract.
  - a) May be anything of value (may be tangible or a promise)
  - b) The two sides can give consideration of unequal value (ie. in the absence of fraud, the actual amount of consideration is irrelevant to formation of contract)

- D. The effect of Duress, Fraud and Misrepresentation on a contract.
1. The doctrine of **Caveat Emptor** is being replaced by modern law requiring that contracts be voluntary and fair.
    - a) Sellers and real estate agents now have an affirmative duty to reveal material defects in the property (Note: This overrides any fiduciary duty to client.)
    - b) Contracts signed by a person who has been defrauded or who is under duress or coercion is voidable by that person or by a court.
  2. To prove **Fraud**, one must show:
    - a) That there was an intentional misstatement,
    - b) Of a material fact,
    - c) That was justifiably relied upon by the defrauded party; encouraging him/her to enter into the contract, and
    - d) Damage
  3. Giving only partial truth may be fraud if there was an intention to misinform.
  4. Personal opinion, even "puffing" is not fraud.
  5. **Misrepresentation** or Negligent Misrepresentation has same elements as Fraud except it was not intentional, just negligent.
  6. A contract may be void or voidable if there is confusion as to its material facts
    - a) Unilateral Mistake - voidable by the injured party who if sued could claim lack of voluntary assent; some courts say it's no defense
    - b) Bilateral Mistake - no "meeting of the minds" and the contract is **VOID**.
- E. The Statute of Frauds
1. The Statute of Frauds requires that certain contracts must be in writing, and signed by the person(s) to be charged to be enforceable in court.
  2. Contracts that are covered under the Statute of Frauds:
    - a) Any contract that conveys any interest in real estate (example: deeds, options, purchase and sales agreements, land installment contracts).
    - b) Any contracts for more than one year (example: 18 month lease).
- F. Performance of the Contract
1. Competent parties may agree to anything in a contract, as long as it's legal.
  2. Most contracts are totally unaffected by the death or insanity of either party.
    - a) Exception: personal services contracts
    - b) Exception: when the parties agree that death or insanity will terminate agreement
  3. Most contracts have a "reasonable period of time" for performance - even when a time is specified.
  4. A "time is of the essence" clause, however, requires that the contract must be performed within the stipulated time.
- G. Assignment and Novation
1. **Assignment** - the transfer of rights and obligations under a contract to a third party. Any contract can be assigned unless there's a clause in the contract forbidding assignment, or it's a personal services contract. NOTE: Assignment does not of itself extinguish liability of the assigning party.
  2. **Novation** - the substitution of a new contract for an existing contract (all parties must discharge prior agreement) NOTE: Novation usually results in relieving the original party of liability.
- H. Discharge of a Contract
1. Mutual agreement.
  2. Complete performance - or sometimes even substantial part performance.

3. Lapse of a "reasonable time".
  4. Destruction of the object of the contract.
  5. Impossibility of performance (act of nature).
  6. The other party frustrating or preventing performance.
  7. Death or insanity (only in personal services contracts).
  8. Bilateral mistake of a material fact.
- I. Breach of Contract and Rights of the Parties
1. Default by the Seller - the Buyer may:
    - a) **Rescind** the contract and recover the earnest money
    - b) Sue the seller for **specific performance**.
      - (1) Court orders performance of the contract at their discretion
      - (2) The object of the contract must be unique
      - (3) Real estate is always considered to be unique
    - c) Sue the seller for **compensatory damages**
      - (1) Buyer must minimize her losses (“mitigate damages”)
      - (2) Damages limited to actual monetary loss
  2. Default by the Buyer - the Seller may:
    - a) Declare the contract forfeited and retain the earnest money as **liquidated damages**: damages that the parties agree to in advance under the terms of the contract (another example: the rental security deposit in a lease)
    - b) Sue the buyer for **compensatory damages**
    - c) In certain cases a Seller may also seek **specific performance or rescission**.

## II. Contracts Used in the Real Estate Business

- A. Brokers and salespeople working under the supervision of a broker can prepare only listings and purchase and sales agreements. Some states do not allow real estate licensees to prepare sales agreements between buyers and sellers. Most states expect the agents will simply fill in the blanks on forms provided by trade association or drafted by attorneys. Brokers or salespeople are **not to "practice law"** (example: can't prepare deeds, title opinions, give zoning advice, etc.).
- B. Listing Agreements may be prepared by the broker as a party to the contract therefore not practicing law
- C. Sales Contracts (Purchase and Sales Agreements, P & S Agreements)
  1. Sales contracts can be prepared by the broker as an agent. The broker is not a party to a P&S Agreement therefore is very limited to what is written by the Brokerage.
  2. The sales contract sets forth all of the details of the agreement between a buyer and a seller for the purchase and sale of property.
- D. The Formation of a Sales Contract
  1. The offer becomes or "ripens into" a sales contract.
  2. The deposit (earnest money or binder) is evidence of the buyer's intention to carry out the terms of the contract.
    - a) To avoid commingling, the earnest money must be held in trust/escrow.
    - b) May be monetary or "in kind" - agreed upon by the buyer and seller and described in the sales contract.
    - c) Must be of a sufficient amount to protect the seller and lessen the chance of buyer's forfeiture.
  3. The offer can be withdrawn at any time prior to acceptance, and the earnest money returned.

4. Acceptance - there must be an acceptance to create a sales contract
  - a) When accepted, the contract is created and a signed copy must be given to all of the parties.
  - b) Notification of acceptance must be given to the party who made the offer before the contract is considered created.
  - c) The sales contract gives the buyer "**Equitable Title**" meaning that the buyer has a right to receive legal title in the future (usually at the closing when the deed is delivered).
    - d) The sales contract also promises that the buyer is to receive "marketable record title" meaning that there are no "clouds" on the title
- E. **Liquidated Damage Clause** specifies that the earnest money will be used by the seller as pre-agreed damages if buyer breaches.
- F. Parts of a Sales Contract
  1. Identification of the parties.
  2. Legal description of the property.
    - a) The property and any conditions affecting its title must be very specifically described.
    - b) Any appurtenances which "attach to and run with the land" must be described.
    - c) Any confusion in the property description could void the contract.
  3. The provisions for any contingencies in the contract.
  4. The type of deed the seller will give.
  5. Any personal property which will be included in the sale. Any personal property (chattel) will be conveyed at the closing by delivery of a bill of sale.
  6. Any fixtures which will be removed by the seller before the buyer takes possession should be specified.
  7. The provisions of the closing and the transfer of possession to the buyer.
- G. The Signing (Execution) of the Sales Contract
  1. The sales contract is signed by the seller, and anyone else who has an ownership interest in the property, and by the buyer(s).
  2. An **attorney-in-fact** (agent appointed by power of attorney) may sign for either the buyer or seller.
- H. The condition of the property at the closing must be the same as when the sales contract was signed. If a long time has lapsed between the signing of the sales contract and the closing, normal wear and tear on the property will be acceptable.
- I. Option Agreements
  1. An **option** is a contract granting the right to buy or lease property at a fixed price within a stated period of time
  2. The optionee gives consideration and has a right to:
    - a) Buy or lease the property for the option price/time.
    - b) Let the option expire.
    - c) Also may try to renegotiate a better deal, but that would not be binding unless agreed to by the optionor.
  3. The optionor is the only party bound prior to exercise. (S)he must:
    - a) Reserve the property for the optionee only.
    - b) Sell or lease the property for the option price if the optionee exercises the option within the option time.
    - c) Any sale of the property prior to termination of the option would be subject to the option.

4. If the optionee exercises her rights under the terms of the option, then both of the parties are bound.
  5. Compare and contrast: **right of first refusal**
- J. Land Contract (**Land Installment Contract**/Contract for a Deed)
1. Buyer purchases the property by making installment payments.
  2. Seller keeps legal title to the property while the payments are being made.
  3. When the terms of the contract have been met and an agreed upon number of payments have been made, the seller delivers a deed giving legal title to the buyer.
  4. During the time of payment, the buyer has equitable title and possession; as well as the responsibility for paying principal, interest, real estate taxes, insurance, and maintenance and repairs on the property.
- K. **Rescission** (disaffirming or voiding a contract).
1. Breaking the contract apart and returning the parties to the position they were in prior to making the contract (status quo ante).
  2. Most states provides statutory rights of rescission ("cooling off periods") for real estate transactions involving condominiums and for sales of timeshares.

Some additional contract principles to discuss:

1. Provisions which are unconscionable.  
Some contractual provisions will be struck down or not enforced when the court deems them to be patently unfair and unreasonable.
2. Parol evidence rule.  
Absent a clear ambiguity, extrinsic evidence (such as oral statements) may not be introduced to vary or contradict written contractual provisions.
3. Contracts of adhesion.  
Courts may relieve consumers from the adverse effects of unfair and/or unreasonable contractual provisions which are included industry wide such that the consumer never really had any actual bargaining power to object.
4. Duty of good faith and fair dealing. All parties to contracts are bound by this duty.
5. Rule of construction: in the face of an ambiguity, a court may rule against the drafting party.

# SESSION THREE

## TRANSFER OF TITLE

Title means the ownership of real property (bundle of rights); and an alienation is the conveyance or transfer of real property, or an interest or right in real property.

- I. **Voluntary alienation** – usually transfer by gift or sale using a specialized contract called a deed
- A. Prior to the transfer of title the legal status of the title should be determined by a search of the land records (title search).
    - 1. The person conveying the property (grantor) must be the (owner of record).
      - a) There should be a clear succession of owners (chain of title).
      - b) There should be no (gaps) in the chain of title.
      - c) The title should be free of encumbrances, liens, litigation, etc. (clouds on the title).
    - 2. Notwithstanding the foregoing, the buyer may legally accept the property as is and it will be a legal transaction.
  - B. The grantee of the property would receive a report from the title company, or attorney doing the title search
    - 1. Abstract of title - a history or digest of all the documents in the land records that affect the property.
    - 2. Title Opinion (Certificate of Title) - prepared by the attorney certifying the legal status of the title, based on the search of the land records.
  - C. There are problems in the land records, however, that could not be discovered in even the most diligent search. To protect the grantee or lender (mortgagee) from defects such as forgery, recording errors, deeds signed by incompetents or under duress, etc.; title insurance is now widely used.
    - 1. Title Insurance does not cover:
      - a) Defects and liens listed in the policy.
      - b) Defects known to the buyer (unless you get **affirmative coverage** to cover these).
      - c) Changes in land use caused by zoning.
    - 2. The two most common policies are the owners' policy, and the lender's (mortgagee's) policy:
      - a) Owner's title insurance protects the owner forever. The premium is paid once - usually at closing.
      - b) Lender's insurance protects the lender for the term of the mortgage. The premium is paid once - at the beginning of the loan.
  - D. The final act of conveyance is the intentional delivery of the deed by the grantor of the property to the grantee. **DELIVERY IS THE LAST ACT OF CONVEYANCE**. There is a legal presumption of acceptance. This presumption may be rebutted.
    - 1. A deed is a contract which is designed to convey an interest in real property requires all of the essential elements of a contract.
      - a) Deeds are subject to the Statute of Frauds.
      - b) Brokers and salespeople are not authorized to prepare deeds.
    - 2. Requirements for a valid deed and conveyance:
      - a) The parties must be legally competent and unquestionably identified.
      - b) The property must be unquestionably identified.

- c) There must be a consideration clause, acknowledging grantor's receipt of value in return for the property.
  - d) Granting clause must show grantor's intention to convey the property
  - e) **Habendum clause** - (To have and to hold) clause acts to define the ownership conveyed to the grantee. This repeats the granting clause.
  - f) Warranties and representations of the grantor, if any.
  - g) Grantor's signature only as (party to be charged) under the statute of frauds.
  - h) All of the above PLUS delivery = CONVEYANCE.
3. Deed requirements for recording:
- a) Valid Deed and Conveyance.
  - b) **Acknowledgement.**
  - c) Deeds are not required to be recorded to be effective as to the parties to it.
  - d) Whether an unrecorded deed is effective against a third party is a matter of state law – states usually follow race, race-notice, or notice theories.
4. Types of deeds:
- a) General Warranty Deed- the grantor covenants to defend the grantee's interests against the whole world (provides the greatest protection for the grantee).The covenants of a general warranty deed include:
    - 1) Covenant of seisin (fee simple title)/ownership and possession of property with the right to sell.
    - 2) Covenant against encumbrances - the deed is free from all liens and encumbrances except those stated in the deed.
    - 3) Covenant of Quiet Enjoyment - the grantor assumes responsibility of protecting the title against the claims of third parties.
    - 4) Covenant of Future Assurance - the grantor will furnish whatever is needed to make the title good.
    - 5) Covenant of Warranty - the grantor is liable for reimbursing the grantee for any title interest lost in the future.
  - b) Special Warranty Deed- warrants only that the title was not encumbered while the grantor held it except as noted in the deed. Any additional warranties must be stated in deed.
  - c) Bargain and Sale Deed - contains only an implied warranty that the grantor has title (ownership) of the property, and possession. It makes no further warranties unless specifically stated.
  - d) Quitclaim Deed - Makes no warranties; not even a covenant that the grantor has title or possession- affords the grantee the least protection. This is often used to release property interests.
  - e) Fiduciary Deed- Deed given by an estate. Example: Executor's Deed.
  - f) Deed in trust- used by a trustor (also called settlor) to convey property to a trustee for the benefit of a beneficiary - usually accompanied by a trust agreement regulating the trustee's actions.
  - g) Trustee's deed- used to convey property out of a trust pursuant to authority granted in the trust agreement.
  - h) Reconveyance deed- executed by the Trustee to return title property held in trust to the Trustor.

E. Voluntary Alienation also includes transfers at death – “devises”

F. Dedication – giving property or interests in property to public for public use (eg. a developer “dedicates” a subdivision road system to the town)

- II. **Involuntary Alienation** – property conveyed without the owner's consent by operation of law
- A. **Eminent Domain** -The legal theory or doctrine that allows the government to take private property for public use. Recently the Supreme Court expanded the definition to include private use benefitting the public, thus decreasing the rights of private ownership.
    - 1) The actual taking of the property is called condemnation.
    - 2) When property is condemned under eminent domain the government must pay the property owner just compensation.
  - B. To satisfy debts - the debt is foreclosed, the property is sold, and the proceeds of the sale are applied to pay off the debt.
  - C. **Escheat**- When property is abandoned, or the owner dies intestate and there are no heirs; title to his/her real estate would pass to the state.
  - D. Land can be transferred by natural forces, as well as the legal process:
    - 1. **Accretion**- The deposit of soil, silt, rock, etc. washed up naturally from a river, ocean, or lake which increases the size of an owner's property.
    - 2. **Erosion** – The gradual loss of soil by the action of water or wind.
    - 3. **Avulsion**- The sudden tearing away of land from a person's property by floods, earthquakes, volcanoes, etc. Usually this is a change in nature of land only.
  - E. **Adverse Possession** – Hostile possession and control of another person’s property
    - 1. OCEAN – open, continuous, exclusive, action and notorious
    - 2. Must not be with permission of owner
    - 3. **Continuity required varies with each state (often 7 to 20 years); “tacking”** is allowed (this allows successive owners to combine their adverse time elements).
    - 4. Adverse possession is a transfer of TITLE by operation of law. The claimant may end up having to sue the owner in an **action to quiet title** to get the interest documented.
    - 5. Compare **Prescription** which is the hostile acquisition of an EASEMENT.

## ESTATES IN LAND

Estates in land are different ways of owning and/or possessing real estate. There are two categories of estates in land: freehold and non-freehold estates.

- I. **Freehold Estates**-when the holder actually owns the property, as well as the right to physical possession. Freehold estates are for an indeterminable period of time.
  - A. Freehold estates in the United States are possible because of our allodial system, allowing individuals to own property free and clear of any rent or service due the government.
  - B. Before private ownership was created by the allodial system, the king or government held title to all of the land under the feudal system.
- II. Types of Freehold Estates (transfers by deed)
  - A. **Fee Simple** - The owner has the full bundle of rights.
    - 1. The highest estate recognized by law.
    - 2. A fee Simple continues for an indefinite period of time, and can be devised (conveyed in a will to the owner's heirs).
  - B. **Defeasible fee** (qualified determinable or base fee) in the future by the occurrence or nonoccurrence of a specific event. Like the fee simple, a defeasible fee lasts for an indefinite period of time and can be devised (ie. conveyed via will).
  - C. **Life Estate** - The ownership interest lasts only for the lifetime of the owner, or the life of

some other designated person (estate pour autre vie).

1. The owner of the life estate (life tenant) has all of the rights of ownership during the lifetime of the designated person; however...The life tenant may not commit waste.
2. A life tenancy may not be devised because it automatically passes to someone else after the death of the life estate owner.
3. **Future interests** - determine what happens to a life estate when its owner dies:
  - a) When the estate reverts back to the original grantor, it's called a reversionary interest.
  - b) When it passes to a third party instead of reverting to the original grantor, it's called a remainder interest and the party receiving it is called a remainderman

D. Legal life estates and other interests

1. Dower - a wife's life estate interest in the real property of her deceased husband.
2. Curtesy- a husband's life estate interest in the real property of his deceased wife.
3. While a spouse is still alive, dower and curtesy are only expectancy, or inchoate interests.
3. Homestead rights – equity in a personal residence protected from creditors for benefit of spouse and children. Amount determined by state law.

III. Forms of property ownership

A. **Ownership in severalty** - ownership by one person.

B. Co-ownership (**concurrent ownership**) - ownership by two or more owners. Each owner has an undivided interest in the property

1. **Tenancy in Common**

- a) Multiple owners can own unequal shares.
- b) The shares don't have to come from the same grantor at the same time.
- c) There is no survivorship (each owner can devise his/her interest).
- d) Example: The common areas in a condo complex are owned by the owners of the condos as tenants in common.
- e) Default rule for concurrent owners, except for married persons
- f) Subject to probate upon death

2. **Joint Tenancy**

- a) Multiple owners must own equal shares.
- b) The shares must come from the same grantor at the same time.
- c) There is survivorship (owners can't devise their interests).
- d) Characterized by the four unities (title, time, interest, possession)
- e) Avoids probate upon death
- f) **Right of Partition** - in both of these concurrent estates the owners can agree to break the ownership apart and take their individual shares of the property to own in severalty (partition).

3. **Tenancy by the Entirety**

- a) Reserved for husband and wife, or civil union partners
- b) Has incidents of survivorship
- c) Interest may be conveyed **ONLY** with the agreement of **BOTH** parties
- d) Upon death of one spouse/partner it automatically reverts to severalty ownership
- e) Upon divorce it automatically reverts to tenancy in common

4. **Ownership in trust** - when property is placed in name of trustee

- a) The parties in a trust
  - 1) Trustor- the person who creates the trust by giving the property to be held by the trustee. Also known as “**settlor**” of trust.

- 2) Trustee - owns and manages the property for the benefit of the beneficiary. A trustee (escrow agent) is a fiduciary
- 3) Beneficiary - the person who benefits from the trust.
- b) Generally used in estate and asset planning and management
- 5. Ownership by business organizations
  - a) Partnerships - two or more persons co-own the business and share in the profits and losses.
    - 1) The two types of partnerships:
      - A) General partnerships - all the partners participate in the operation and management of the partnership; and share personal liability for the business obligations of the partnership.
      - B) Limited partnerships - one or more general partners set up and manage the partnership and is/are personally liable for its business losses. Limited, or silent partners don't participate in the management of the business and are liable only to the extent of their investment in the business.
  - b) Corporations - Legal entities (persons) created under state law. Corporate shareholders are provided with limited liability.
  - c) Limited Liability Companies – Legal entities (persons) created under state law. Flexible rules: may mimic partnership OR corporation. KEY question for agent is whether LLC is manager or member managed.
  - d) Syndicates - A joining together of two or more persons or business entities to create and operate a real estate investment.
    - 1) A syndicate may take many legal forms, such as joint tenancies, tenancies in common, corporations, joint ventures, trust, etc.
    - 2) The most common forms used, however, are general and limited partnerships.
    - 3) Syndicates are regulated by:
      - a) Securities and Exchange Commission (S.E.C.) - if the syndicate shares will be sold between the states.
      - b) State securities laws (**Blue Sky Laws**) - if the shares will be sold solely within one state.

#### IV. Condominium, Cooperative, and timeshare ownership.

- A. **Cooperative** - Shareholders in a corporation which owns an apartment building can use units in that building because they own stock in the corporation.
  - 1. The cooperative corporation holds title to the land and building
  - 2. The shareholders own stock (personalty), and are given a proprietary lease to their unit.
  - 3. Taxes and mortgages are liens against the corporation.
- B. **Condominiums**- Fee simple ownership of the air space of a particular unit; with the owner also owning an interest in the common area as tenants in common with the other owners.
  - 1. The owner records his/her ownership in the land records.
  - 2. A condo may be mortgaged, and the owner subject to real property taxes.
  - 3. If a unit owner defaults in his/her mortgage or tax payments, or in the payment of condo fees, a foreclosure sale of that owner's unit can result without affecting the title of the other owners.

- C. **Timeshare** ownership - a form of communal (“interval”) ownership which allows multi-owners to use the property for a variable or fixed time period.
1. Can be conveyed by a deed as actual fee simple ownership, or by a lease giving the right of possession.
  2. Owner can purchase either a floating (variable) time period or the right to a specific time frame each year.
  3. Nickname: prepaid vacation.
  4. Time share estate: fee ownership
  5. Time share license: lease
- V. **Non-freehold estates** (leaseholds) - conveyance by demise giving the tenant only the right to possess the property. Leaseholds are usually considered personal property (**Chattel Real**)
- which
- A. Types of non-freehold estates
1. **Estate for years** - a lease for a specific duration, with no automatic renewal.
  2. Estate from period to period (**periodic tenancy**) - a tenancy for a specific period, automatically keeps renewing for similar succeeding periods until one of the parties gives notice to terminate.
  3. **Estate at will** - a tenancy for an unspecified or uncertain duration - terminated by either party giving proper notice.
  4. **Tenancy at sufferance** - the tenant holds over after the lease has expired, without permission of the landlord. A holdover tenant is not legally a trespasser.
- B. Breach of lease
1. Covenant of **quiet enjoyment** - an implied warranty that the tenant has the right to possess enjoy the leased premises without interference of the landlord.
  2. **Constructive eviction** - The landlord forces the tenant off of the property by making the premises uninhabitable. In modern statutes relating to residential leases this is replaced with the warranty of habitability.
  3. Tenant may not commit **waste** (ie. substantially change property)
    - a) Minor repairs necessary to protect the property may be required, but major repairs are not.
    - b) Forms of waste include the following:
      - 1) Affirmative – negative waste, tearing down building
      - 2) Permissive – negative waste, failing to make minor repairs
      - 3) Ameliorating – improves value, but done without permission
  4. Suit for possession - **actual eviction**
    - a) Landlord must serve tenant with a notice to quit.
    - b) Landlord initiates eviction proceeding in court.
    - c) Court issues a **writ of possession**.
    - d) Landlord not allowed to use **distrain**.
- C. Landlord's liability for injuries on premises.
1. Generally, **caveat emptor** still applies here - the tenant cannot sue.
  2. There are two exceptions:
    - a) Landlord is liable for injuries which occur in the common areas
    - b) Landlord is liable for injuries occurring in the leased unit caused by hidden defects that landlord knew about but tenant was unaware.
- D. Assignment and subleasing
1. Assignment - when the tenant transfers all of his or her leasehold interests.
  2. Subleasing - When the tenant transfers less than all of the leasehold interests by leasing them to a new tenant.

3. Usually, neither assignment nor subleasing relieves the original lessee of the obligations to make rental payments.
  4. Both assignment and subletting are allowed unless restricted in the lease.
- E. Types of leases
1. Gross lease - the tenant pays a fixed rental amount, but the landlord pays all of the operating expenses of the property.
  2. Net lease - the tenant not only pays a fixed rent to the landlord, but also must pay all or part of the operating expenses of the property.
  3. Percentage Lease- The rent is a percentage of the tenant's business gross income.
  4. Graduated lease - provides for specific rent increase over the term of the lease.
  5. Index lease (escalator clause) - provides a formula for increasing or decreasing rent.
  6. Ground lease – leasing of the land only; tenant will build structure on land – typical arrangement for strip development.

## ENCUMBRANCES

- I. An encumbrance is a right or interest that is held by someone other than the owner of the property. It attaches to, and is binding on the property.
- A. While an encumbrance may lessen the value, or obstruct the use of the parcel...
  - B. It won't necessarily prevent the transfer of title to the property.
  - C. A lien is the right or charge of a creditor or the government against property. It provides security for a debt or obligation of the property owner.
    1. If the debt or obligation of the owner isn't satisfied, then the lien holder has the right to have it paid out of the property - often from the proceeds of a court-ordered sale.
    2. Liens attach to and "run with the property". If the property is later conveyed, any successive owners will also be bound.
    3. Specific liens, like tax liens, special assessment liens, and mechanic's liens, are secured by specific property and only affect that property.
    4. General liens, like judgment liens, I.R.S. liens, and inheritance tax liens can affect all of the property of a debtor.
    5. Some of the types of liens include:
      - a. Tax liens (including I.R.S. and special or betterment assessments, as well as local real property tax liens).
      - b. Judgment liens
      - c. Mechanic's liens (to provide security for tradespersons or suppliers who furnish labor or materials in the improvement of real property)
      - d. Miscellaneous Liens (such as for development of current use property)
      - e. Distinguish *lis pendens* – notice of law suit or claim – not actually a lien
  - D. Use restrictions (restrictive covenants) - private restrictions in deeds created by grant or reservation (Also see Private Land Use Controls, VIII of Land Use Controls below)
    1. Restrictions “run with the land” and will apply until released.
    2. Restrictive covenants cannot be against public policy.
    3. Restrictive covenants are narrowly (strictly) construed.
  - E. Easements - A right acquired by one party to use the land of another party for a particular purpose.
    1. An easement right may be above or below the ground, as well as on the surface.
    2. **Easement in Gross** - is merely a personal right to use the land of another (examples include: railroad rights of way, timber rights, a utility company's right

- of way, etc.)
3. **Appurtenant easement** - an easement that is attached (or appurtenant) to the ownership of a particular parcel of land which allows this owner the right to use a neighbor's land.
    - a. The parcel of land that benefits from the easement is called the dominant tenement
    - b. The parcel of land over which the easement appurtenant runs is the servient tenement.
  4. Easement by necessity - This gives the owner of landlocked property access to the property by implying the right of ingress (entry) and egress (exit) over an adjoining parcel of land.
  5. Easement by **prescription** - State law may award a claimant an easement on property owned by another if the claimant can prove:
    - a. That (s)he had made use of the property for a period of time defined by state law and...
    - b. The use of the property was in a manner that was open, notorious, continuous, exclusive, and adverse to the owner. (See also adverse possession).
  6. License - personal permission to enter the land of another for a specific purpose (examples include a ticket to enter a stadium to see a ball game, or permission to park in a neighbor's driveway, etc.).
    - a. A license differs from an easement in that it can be terminated or cancelled by the licensor.
    - b. Compare a **license coupled with an interest**, which may not be terminated until the improvement is exhausted. Example: spring right granted by permission but not by formal easement, where benefitted party expended money to establish spring in reliance on the permission
  7. **Encroachment** - When a building or some other improvement illegally extends over a boundary line into a neighboring property.

## SESSION FOUR

### FINANCING

Many of the customers and clients that you will be dealing with will need help arranging the financing they need to make their purchases. Generally, they will become involved in a mortgage situation.

- I. The mortgage loan:
  - A. **Mortgagor** (borrower) receives the loan and gives a mortgage deed to the mortgagee (lender) as security for the debt.
  - B. The **mortgagee** holds the security interest given in the mortgage deed until the loan is paid off; and then returns the security interest back to the mortgagor.
- II. A mortgage situation also requires the mortgagor to give the mortgagee a mortgage note, along with the mortgage deed. The mortgage note contains the mortgagor's promise to repay the loan. Here are the terms of the two contracts that the mortgagor (borrower) gives to the mortgagee

(lender) - the mortgage note and the mortgage deed:

- A. The note (mortgage note/**promissory note**) is a personal obligation, and it evidences the debt.
  1. Of the two contracts that the mortgagor gives, the note is the document of primary importance.
  2. The parties must be identified, but only the mortgagor (maker/obligor) signs. Liability may be "**joint and several**".
  3. Contains the amount of the debt payable to the lender, the time and method of payment, and the rate of interest. The interest rate is subject to **usury laws**.
  4. Contains the maturity date (due date), and any balloon payment provisions.
  5. Would contain any discount points charged by the lender to increase its yield, and/or cover the costs of originating the loan (**origination points**). Each point equals 1% of the loan and on a 30 year mortgage increases lender's yield 1/8%.
  6. Pre-payment clauses and acceleration clauses would be included in the note
  7. Assignment clauses, **alienation (due-on-sale) clauses**.
  8. The money market defines the terms and conditions agreed to in a mortgage note.
- B. The mortgage deed conveys an interest in the mortgagor's property as security for the loan, and is of secondary importance.
  1. A mortgage deed is not to be confused with the deed given by seller to convey legal title to the buyer/mortgagor.
  2. Requires all of the elements of a deed.
    - a. A mortgage deed is under the Statute of Frauds.
    - b. Signed only by the mortgagor (as grantor).
  3. The mortgagor/grantor of the mortgage deed is required to make covenants in the deed to protect the security interest of the mortgagee.
    - a. These covenants would include: keeping the property insured, paying the property taxes, paying principal and interest, keeping the property in good repair, and not "**committing waste**" on the property.
    - b. A breach of any of these covenants in the mortgage deed would entitle the mortgagee to foreclose.
  4. Even though (s)he gave a security interest to the mortgagee in the mortgage, the mortgagor keeps possession of the property, and is entitled to any rents and profits produced by the property. This is **hypothecation** - pledging property as security for a loan without giving up its possession.
  5. Unless there is a "due on sale" provision, the mortgagor can always convey the property to a new buyer, who "assumes" the loan, or buys the property "subject to" the mortgage.
    - a. **Assuming the loan** - buyer assumes liability along with the original mortgagor for payment of the entire debt.
    - b. Subject to the loan - buyer doesn't take liability for entire debt.
  6. Some states require that the lender only be given a lien on the property, or that a trustee (rather than the mortgagee) hold the security interest.
  7. The title is given to the mortgagee, however, "subject to a condition subsequent" (defeasance clause), and the lender's interest can be defeated in the future when the loan is repaid.

### III. Different types of Mortgages

- A. D.V.A. (Department of Veterans Affairs) - from DVA approved lenders for eligible veterans or their eligible dependents.

1. For purchase of:
  - a. Single Family and Multi-family dwellings up to four units,
  - b. New/used mobile homes and lots for mobile homes,
  - c. New condos and construction of condos,
  - d. To refinance existing loans,
  - e. For purchase/construction/repair of homes.
2. Loan conditions:
  - a. 100% financing possible
  - b. Interest rate set by money market as of 10/92-prior to 10/92 DVA did.
  - c. Property must be appraised by DVA approved appraiser who prepares a "Certificate of Reasonable Value: - the amount of the guarantee is based on the amount of the "CRV" or the selling price, whichever is less.
  - d. Both seller and buyer can pay points on DVA loans generated after October, 1992 before that date seller had to pay points
  - e. Loans must come from regular institutional sources.
  - f. Closing costs may not be financed.
  - g. Guarantee is usually limited to 25% of the loan, or \$104,250, whichever is less, and gives the "lending institution" the security of a down payment.
  - h. Newer DVA loans (given after 3/1/88) can be assumed only if the DVA or the lending institution approves of the assumption.
    1. The loan may be assumed by a non-veteran.
    2. The original mortgagor/veteran whose loan is being assumed by an approved buyer will be released from the liability of the loan.
  - i. To qualify for a DVA loan, a borrower must:
    1. Get a Certificate of Eligibility from the DVA.
    2. Have the property appraised by a DVA-approved appraiser.
    3. Have good credit.
    4. Sign a statement that (s)he will be an owner/occupant of the property.
  - j. Veteran must occupy the property.
  - k. There is no prepayment penalty on a DVA loan provided 30 days notice is given.
- B. FHA (Federal Housing Administration) - insured loans made by FHA approved lenders.
  1. FHA is now part of HUD (The Department of Housing and Urban Development).
  2. Loans come from approved regular institutional sources.
  3. Interest rate set by money market.
  4. Property must be appraised by an FHA approved appraiser.
  5. **Section 203(b) program**; small downpayment required
  6. The borrower pays the FHA insurance premium (MIP) in two parts: an up-front premium either at the closing or financed into the loan amount AND an annual premium which is charged monthly.
  7. Both buyer and seller may pay the discount points.
  8. Newer FHA loans can be assumed only by buyers who are approved by the FHA or lending institution.
  9. No pre-payment penalty is allowed in FHA insured loans provided 30 days notice is given.
- C. Rural Development (RD) formally known as Farmers Home Administration (FmHA) - loans which come directly from the federal government (U.S. Department of Agriculture).

1. Can be used for the purchase, construction or improvement of primary residential, single family dwellings only.
  2. Dwelling must be located in a rural area (20,000 population or less).
  3. The U.S.D.A. sets the loan amount and the interest rate.
  4. No down payment is required.
- D. Conventional mortgages defined as mortgages not backed by a Federal Agency. These mortgages are privately insured for any mortgage amount representing more than 80% of the appraised value of the property. Borrower is charged the market interest rate plus the insurance premium (PMI) costs. Loans originated after July 1999 are subject to federal law requiring termination of PMI coverage when borrower has accumulated 22% equity based on the purchase price of the home.
- E. Ratios vary according to the type of mortgage obtained. "Ratios" are defined as the relationship of debt-to-income. This determines whether loans are "conforming."
- | MORTGAGE PROGRAM | HOUSING EXPENSE (PITI) | TOTAL DEBT |
|------------------|------------------------|------------|
| Conventional     | 28%                    | 36%        |
| FHA              | 29%                    | 41%        |
| VA               | ----                   | 41%        |
- F. Consider the effect of recent regulations promulgated by the **Consumer Financial Protection Bureau (CFPB)** which establishes criteria for "**qualified mortgages**" effective January 10, 2014. In these regulations the general debt ratio is 43%.

#### IV. Variations of Mortgages

- A. **Amortizing Mortgage** - payments include not just interest but also reduce the principal. See Factor Charts in text and/or study guide.
- B. Straight payment (Term Mortgage) - allows for periodic payments of interest only with a lump sum payment of all of the principal at maturity (balloon payment).
- C. Purchase-money mortgage (P.M. Mortgage) - given by the buyer to the seller as all or part of the purchase price (**owner financing**).
- D. Blanket mortgage - covers more than a single property or lot. Borrower would want a "**partial release clause**" to provided for separate releases as property is developed.
- E. Package Mortgage - covers not only a parcel of real property but also all fixtures and appliances located on the property (personal property).
- F. Open-end Mortgage - like an open line of credit, it secures future advances of funds given by the lender to a borrower. Additional loans (extensions) given at prevailing interest rates. Examples include **HELOC's**.
- G. Demand mortgage - entire outstanding principal due on the demand of lender.
- H. Construction loans - generally short-term or interim loans used to finance the construction of an improvement. Periodic payments or draws are made by the lender based on work completed. There is an initial loan during construction and a **take-out loan** upon completion of construction in the standard arrangement.
- I. Wrap-around mortgage - A new lender assumes payments of existing loans, and gives the borrower a new increased loan at a higher interest rate. It can be used to consolidate existing loans.
- J. Reverse Annuity Mortgage - Borrower borrows giving equity in his/her home as security for the loan. The funds are released from the lender in periodic payments. Often used by older people to supplement fixed incomes.
- K. Adjustable Rate Mortgage (ARM) - The interest rate may be adjusted either up or down based on a prescribed index. Annual adjustments are the norm.
- L. Graduated Payment Mortgage - Initial payments are low, but are adjusted to increase over

the term of the loan. Section 245 of FHA has similar program.

- V. Sources of real estate financing - the primary mortgage market. (Which of the following is dominant in today's market?)
- A. Savings and Loan Associations -
    - 1. Local in nature
    - 2. Customer deposits insured by the Savings Association Insurance Fund for up to \$250,000 per account as of 2010 (be sure to check changing regulations).
    - 3. Monitored by the Office of Thrift Supervision created by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989.
  - B. Mutual Savings Banks -
    - 1. Mutually owned by their investors (depositors)
    - 2. Active in mortgage market dealing most often in FHA and DVA mortgages.
  - C. Commercial Banks -
    - 1. Specialize in short-term loans, such as construction and home improvement loans.
    - 2. Accounts insured by the Bank Insurance Fund for \$100,000 per account.
  - D. Insurance Companies - Specialize in long-term loans such as commercial and industrial loans.
  - E. Mortgage Banking Companies -
    - 1. Originate loans using funds borrowed from others as well as their own money.
    - 2. Generally service the loans they originate.
  - F. Credit Unions -
    - 1. Cooperative organizations that require membership to borrow.
    - 2. Only recently became a source for long-term loans.
  - G. Mortgage Brokers -
    - 1. Originate loans by acting as intermediaries between lenders and borrowers.
    - 2. They do not service loans.
  - H. Sale of State Mortgage Bonds
    - 1. Authorized by the Federal Government.
    - 2. Low interest rates are usually charged.
    - 3. Designed to benefit low and middle income buyers.
    - 4. Usually for either first-time buyers, or buyers buying in target areas.
  - I. Owner assisted -
    - 1. Purchase money mortgages – consider whether SAFE act would require a mortgage originator's license for the seller to make the loan
    - 2. Land Contracts/Contract for Deed
      - a. Seller remains the owner of record.
      - b. Buyer makes installment payments toward the purchase of the property.
      - c. When a certain number of installment payments have been paid (agreed upon by the buyer and seller), then legal title is given to the buyer.
    - 3. Sale and leaseback - The sale of the property to generate cash and then its immediate lease back so the original owner can keep possession.
      - a. Often, contract provisions allow the seller/tenant an opportunity to buy back the property at a future date.
- VI. The ways of Discharging a Mortgage:
- A. Repaying the debt.
    - 1. Indicated by a release/discharge that the lender uses to reconvey the property that was given as security back to the borrower.

2. The release (satisfaction piece) requires the same legal formalities as the original mortgage deed.
- B. Giving a deed in lieu of foreclosure - Conveying the mortgagor's interests in the property to the mortgagee. The lender's security interest would become a fee simple when combined with the borrower's bundle of rights.
- C. Judicial Action - foreclosure, action to quiet title, etc.

#### VII. Mortgage foreclosure and redemption

- A. When a borrower defaults in making payments, or fulfilling any of the covenants in the mortgage deed, the lender can enforce its rights through a foreclosure. Prior to exercising this right, the lender may be required to give the borrower a **right to reinstate** the loan, ie. pay back only that which is necessary to bring the loan current. If the borrower does not reinstate, then foreclosure may proceed. There are two main methods of foreclosure currently used in most states:
  1. Judicial foreclosure by sale
    - a. Upon default by the borrower, the lender accelerates the due date of all the payments.
    - b. The lender sues the borrower and obtains a judgment and a court order to sell the borrower's property.
    - c. **Equity of redemption** and statutory redemption periods pass. These are opportunities for the borrower to redeem the property by paying off the mortgage plus expenses.
    - d. A public sale is advertised, and the property sold to the highest bidder.
    - e. Sale is confirmed by the court.
  2. Non-Judicial foreclosure – mainly for commercial mortgages
    - a. A power of sale clause is included in the mortgage deed the borrower gives to the lender.
    - b. A notice of default is recorded, and ads publicizing the sale of the property must be published in local newspapers.
    - c. The highest bidder purchases the property at a public sale.
  3. **Deficiency Judgment** - if the property doesn't sell for enough at the foreclosure sale to satisfy the balance of the loan plus foreclosure costs; then the lender can get a personal judgment against the borrower for the unpaid balance.

#### VIII. Secondary Mortgage Market - Usually both the mortgagor and the mortgagee are able to transfer their interests to third parties. The mortgagor is able to convey the property to a third party who buys it either "assuming" or "subject to" an existing loan. The mortgagee may transfer the mortgage to investors in the secondary mortgage market.

- A. Warehousing Agencies in the secondary mortgage market purchase existing mortgage loans and either "warehouse" them to earn the compound interest, or repackage them for sale to other investors.
- B. The major warehousing agencies:
  1. Federal National Mortgage Association - FNMA, or Fannie Mae.
    - a. Privately owned corporation.
    - b. FNMA is the largest investor in the secondary mortgage market.
    - c. Buys, warehouses and sells conventional as well as FHA and DVA mortgages.
  2. Government National Mortgage Association - GNMA or Ginnie Mae.

- a. Government Company - a division of HUD.
- b. Works with FNMA in the secondary mortgage market.
- c. Underwrites special assistance loans for middle and low income housing.
- 3. Federal Home Loan Mortgage Corporation - FHLMC or Freddie Mac.
  - a. A federal agency specializing in the purchase of conventional mortgages.
  - b. Biggest direct player in local secondary mortgage market.

**TRUTH IN LENDING ACT**  
**(REGULATION Z)**

- I. This is federal legislation designed to help consumers compare the costs of borrowing money. Now being regulated by Consumer Financial Protection Bureau.
- II. Regulation Z applies to:
  - A. Loans to individuals for all real estate transactions secured by a residence with no dollar limit.
  - B. Personal loans up to \$25,000 made in the ordinary course of business.
- III. Types of loans exempted from disclosure requirements:
  - A. Business, commercial, and agricultural loans.
  - B. Loans made without interest charges.
  - C. Loans with four (4) or fewer installments.
- IV. Disclosure requirements of Regulation Z:
  - A. The true annual interest rate, as well as all other finance charges must be disclosed to the customer before the transaction is completed.
  - B. The finance charge must be stated as the "annual percentage rate" (A.P.R.).
  - C. The finance charge (A.P.R.) must include interest, loan fees, service charges & finder's fees.
  - D. The lender (or real estate agent) must inform the customer that (s)he has the right to rescind the transaction up to midnight of the third business day following the transaction. In an emergency this right can be waived. Exceptions to this right are as follows:
    - 1. Residential Purchase Money loans
    - 2. First Mortgages
    - 3. Deed of trust loans
- V. **Regulation Z** does not require lenders and brokers to advertise credit terms.
  - A. Very general terms and/or the A.P.R. may be advertised alone without full disclosure of the other terms of the financing.
  - B. If further credit details are advertised, however, the full disclosure of the terms must be made:
    - 1. Amount of the loan.
    - 2. Amount of the down payment.
    - 3. The A.P.R.
    - 4. The number and amount of the payments.
    - 5. The total of all the payments to be made over the course of the loan (unless first mortgage on a dwelling).
- VI. Penalties for non-compliance include a fine of up to \$10,000 for engaging in unfair or deceptive

practices, plus:

- A. CIVIL - liability to the consumer for twice the finance charge up to a maximum of \$1,000.
- B. CRIMINAL - up to \$5,000 fine and/or one year imprisonment.

**REAL ESTATE SETTLEMENT PROCEDURES ACT**  
**(R.E.S.P.A.)**

- I. Federal legislation requiring disclosure to a borrower of closing costs.
- II. Application
  - A. Applies only to transactions involving new first mortgage loans on one (1) to four (4) family residential properties.
  - B. Applies to federally related loans.
- III. Requirements
  - A. Within three (3) days of application, the lender must give a copy of a book entitled "Shopping for Your Home Loan" to each loan applicant.
  - B. Also within three (3) days of application, the borrower must be provided with a good-faith estimate (GFE) of closing costs by the lender.
  - C. The HUD Settlement Statement must reflect the origination fees and transfer taxes reflected on the GFE with ZERO tolerance. Certain other items, as a group, including recording fees and fees for settlement services for which the bank supplied the name to the applicant, need to be within a 10% tolerance. Any excess is owed to the borrower by the lender within 30 days of closing. Lenders are allowed to adjust their GFE and re-disclose the loan particulars in the face of legitimate changed circumstances.
  - D. A copy of the HUD 1 information must be made available to the borrower, if borrower asks, one business day prior to closing.
  - D. The closing statement must be prepared on a HUD form 1 (Uniform Settlement Statement).
  - E. Kickbacks and unearned fees are explicitly prohibited. Section 8 of the Act. It is a crime to breach this. \$10,000 fine and up to one year in jail.
  - F. The charging of fees for the preparation of the RESPA forms is specifically prohibited.
  - G. Mandating the use of a particular title insurance company is prohibited. Section 9 of the Act.

**FOREIGN INVESTMENT IN REAL PROPERTY TAX ACT**  
**(F.I.R.P.T.A) Section 1445**

- I. Federal legislation designed to insure that nonresident foreign sellers and foreign corporations pay U.S. capital gains taxes when they dispose of real property in the U.S.
- II. Requires buyers to:
  - A. Withhold 10% of the purchase price from foreign sellers of U.S. real property, and
  - B. Send the money withheld to the I.R.S.
- III. The broker may be liable for the payment of this tax-limited to the amount of his/her commission.

- IV. This law applies to the transfer of any real property located in the United States.

### **I.R.S. REGULATIONS**

I. Independent Contractor Status vs. Employee Status

- A. The IRS has defined three (3) requirements necessary for an agent to qualify for "independent contractor" status:
1. The agent must have a current real estate license as a broker or salesperson.
  2. Salespeople must have a written contract with their broker which states that s/he "will not be treated as an employee for federal tax purposes".
  3. Most (90%) of the agents' income must be based on sales production, rather than the numbers of hours worked.
- B. If the licensee earns his/her income on an independent basis, rather than for the number of hours worked, property developers, appraisers, managers, etc. would be included under this rule.

II. Informational Returns (Form 1099) (See page 403 of text)

- A. A form 1099S must be filed for sales or exchanges of residences with four (4) or fewer units.
- B. Form 1099 Misc. also required for reporting all real estate commissions, referral fees, and rents collected in excess of \$600/yr.

III. 1031 Tax Deferred Exchanges (See pages 435-436 of text)

- A. Real estate investors can defer taxation of capital gains by making a property exchange.
- B. The tax is deferred, not eliminated.
- C. The exchanged properties must be of "like kind". (commercial real estate for commercial real estate)
- D. Additional capital or personal property included with the transaction to even out the exchange is considered to be "boot" and the person receiving it is taxed at the time of the exchange.

IV. Imputed Interest (playing with ordinary income vs. capital gain)

- A. If an installment contract fails to include an interest rate, or states an unreasonably low rate, the IRS will impute interest at a prescribed rate, computed monthly.
- B. The IRS law on imputed interest does not cover installment sales of less than \$3,000.
- C. The rate for determining the amount of imputed interest is based on the applicable federal rate (AFR).
- D. There are three (3) applicable federal rates (AFRs) used, depending on whether the debt instrument is:
1. Short term - not over three (3) years.
  2. Midterm - over three (3) years, but not over nine (9) years.
  3. Long term - over nine (9) years.

V. Anti-Trust Laws

- A. The real estate business is subject to anti-trust laws which forbid unreasonable restraint of trade.
- B. The two (2) most common anti-trust violations in real estate are:
1. Price-fixing - a conspiracy among real estate brokers to fix prices for their

- services rather than allowing the prices to be established through competition in the market. Even a discussion of commissions between brokers representing different companies is dangerous.
- 2. Allocating of customers or markets between real estate companies in an effort to eliminate competition.
- C. Penalties for violation of the Sherman Anti-Trust Act:
  - 1. CRIMINAL - maximum \$100,000 fine and three (3) years in prison for willful violation.
  - 2. CIVIL - liability for three (3) times the actual damages plus attorney's fees and costs.

### CLOSING THE REAL ESTATE TRANSACTION

- I. Pre-closing Procedures
  - A. Consummation of real estate transaction
    - 1. Promises made in sales agreement fulfilled.
    - 2. Mortgage loan funds distributed
    - 3. Title transferred
  - B. Buyer's issues. The buyer will want to be assured that
    - 1. The seller is delivering good title.
    - 2. The property is in the promised condition.
      - a) Review the title evidence
      - b) Review the seller's proposed deed
      - c) Review any documents regarding removal of liens and encumbrances
      - d) Review the survey
      - e) Review the results of property inspection; deal with objections
      - f) Due diligence on any outstanding leases
  - C. Final property inspection to make certain
    - 1. Necessary repairs made
    - 2. Property is well maintained
    - 3. Fixtures are in place
    - 4. No unauthorized removals or alterations
  - D. Survey – Determine whether state requires survey and/or survey recording
  - E. Seller's issues. The seller will want to be assured that
    - 1. The buyer has obtained the stipulated financing.
    - 2. The buyer has sufficient funds to complete the sale.
  - F. Title procedures
    - 1. The buyer needs to be assured that the seller's property and title comply with the contract requirements.
    - 2. The seller is usually required to show proof of ownership by producing current title evidence (form that is customary in your area).
    - 3. The title or abstract company usually makes two title searches.
      - a) The first shows the seller's status as of the contract date.
      - b) The second is made for the date the deed is recorded.
      - c) The seller may be required to execute an affidavit of title.  
In areas where closed in escrow, not needed.

- II. Conducting the Closing
  - A. Terminology varies by geographic region
    - 1. Settlement and transfer
    - 2. Passing the papers
    - 3. Escrow
  - B. Face-to-face closing—the gathering of the parties interested in the real estate transaction at which the promises made in the real estate sales contract are kept or executed
    - 1. Two closings can occur
      - a) The closing of the buyer's loan
      - b) The closing of the sales transaction
    - 2. May be held at the title insurance company, the lending institution, one of the parties' attorneys' office, the broker's office, the registry of deeds or the escrow company
    - 3. May be attended by the buyer, the seller, the broker, the attorneys, a representative of the lending institutions involved, a representative of the title insurance company
    - 4. The settlement agent or closing officer - the person who presides over the closing.
    - 5. The delivery of deed is made when all parties are satisfied that everything is order.
  - C. Closing in escrow
    - 1. The method of closing in which a disinterested third party is authorized to act as the escrow agent and coordinate the closing activities.
    - 2. Because the escrow agent is placed in a position of trust, many states have laws regulating escrow agents and limiting who may serve in this capacity.
  - D. Escrow Procedure
    - 1. After escrow agent selected and contract signed, broker deposits earnest money with escrow agent.
    - 2. Before the closing, the seller will deposit with the escrow agent
      - a) The deed conveying the property to the buyer
      - b) Title evidence (whatever is customary in your area)
      - c) Existing hazard insurance policies
      - d) A letter from the lender and an **estoppel certificate** stating the exact principal remaining if the buyer is assuming the seller's loan
      - e) Affidavits of title (if required)
      - f) A **reduction certificate** (payoff statement) if the seller's loan is to be paid off
      - g) Other documents necessary to clear the title or complete the transaction
    - 3. Before the closing, the buyer will deposit with the escrow agent
      - a) The balance of the cash needed to complete the purchase, usually in the form of a certified check
      - b) Loan documents if the buyer is securing a new loan
      - c) Proof of hazard insurance, including, if required, flood insurance
      - d) Other documents necessary to complete the transaction
    - 4. The escrow agent is given the authority to examine the title evidence
      - a) If the title is marketable and all other conditions are met, the escrow agent will disburse the funds and record the documents.
      - b) If the title has liens, they will be paid off first.
      - c) If the sale cannot be completed, the parties will be restored to their former status.

- F. IRS reporting requirements—**Form 1099-S**
    - 1. Contains the seller's social security number, gross sales price and the amount of property tax that was reimbursed to the seller by the buyer (seen as income by the IRS)
    - 2. Must be filed by the settlement agent (identified on HUD Settlement Statement)
  - G. Broker's role at closing - varies from simply collecting the commission to conducting the proceedings
  - H. Lender's interest in closing - to protect its security interest in the property, the lender can require
    - 1. A title insurance policy
    - 2. A fire and hazard insurance policy
    - 3. A survey
    - 4. A termite or other inspection report
    - 5. A certificate of occupancy (for newly-constructed buildings)
    - 6. Reserve or escrow accounts for tax and insurance payments (impounds)
    - 7. Representation by its own attorney at the closing
- III. RESPA Requirements – Review and more information
- A. Purpose
    - 1. To provide consumers with greater and more timely information on the nature and costs of settlement
    - 2. To eliminate "kickback" and other referral fees that tend to unnecessarily increase the costs of settlement
  - B. RESPA requirements must be complied with when the purchase of a one-to-four-family residential unit is financed by a federally-related new first mortgage loan
    - 1. Made by a federally-chartered lending institution
    - 2. Made by an institution whose deposits are federally-insured
    - 3. FHA-insured
    - 4. VA-guaranteed
    - 5. Administered by HUD (soon to be Consumer Financial Protection Bureau)
    - 6. Intended to be sold to Fannie Mae, Ginnie Mae, or Freddie Mac
  - C. Exceptions to the "new loan" requirement
    - 1. Purchase money mortgages
    - 2. Installment sales (land contracts)
    - 3. Buyer's assumption of existing mortgage
    - 4. No exception if
      - a) The terms of assumed loans are modified
      - b) Assumed loans for which the lender charges more than \$50 for the assumption
  - D. Controlled business arrangements (CBAs)—affiliated firms offer package of services to consumers.
    - 1. The relationship between the firms must be disclosed in writing to consumers.
    - 2. Consumers must be free to obtain the services elsewhere.
    - 3. Fees are not exchanged among the affiliated companies simply for the referral of business.
  - E. Disclosure requirements
    - 1. The lender must give a copy of special informational HUD booklet to every person from whom they receive or for whom they process a loan application.
    - 2. Within three business days of the loan application, the lender must provide the

- borrower with a good-faith estimate (GFE) of the settlement costs the borrower is likely to incur.
    - 3. The loan closing information must be prepared on the Uniform Settlement Statement (HUD Form 1) and available for inspection at or before settlement.
    - 4. GFE must be accurate
      - a) Zero tolerance for origination fee and transfer tax
      - b) Ten percent group tolerance for referred services and recording fees
  - F. Kickbacks and referral fees
    - 1. Kickbacks and *unearned* referral fees are prohibited.
    - 2. The payment or receipt of any fee or thing of value where no service is actually rendered is prohibited.
    - 3. Criminal violation: \$10,000 fine and/or up to one year in jail
  - G. No mandating usage of a particular title insurance company
- IV. Preparation of Closing Statements
  - A. How the closing statement works
    - 1. A debit is a charge (an expense).
    - 2. A credit is an amount entered in a person's favor.
  - B. The buyer's debits and credits are totaled; when the credits are subtracted from the debits, the difference is the cash the buyer must bring to the closing.
  - C. The seller's debits and credits are totaled; when the debits are subtracted from the credits, the difference is the amount the seller will receive at closing.
  - D. Expenses include
    - 1. Broker's commission
    - 2. Attorney's fees
    - 3. Recording expenses
    - 4. Transfer tax
    - 5. Title expenses
    - 6. Loan fees
    - 7. Tax reserves and insurance reserves (escrow or impound accounts)
    - 8. Appraisal fees
    - 9. Survey fees
    - 10. Additional fees and prorations
- V. Proration - expenses divided between the seller and the buyer, including accrued items (such as real estate taxes) and prepaid items (such as fuel oil in a tank)
  - A. The arithmetic of prorating
    - 1. Four considerations
      - a) The nature of item being prorated
      - b) Whether it is accrued item requiring determination of earned amount
      - c) Whether it is prepaid item that requires the unearned amount refunded
      - d) What arithmetic processes must be used
    - 2. Items for which credit and debit are swapped between seller and buyer are set forth on page 1 of the HUD Settlement Statement
  - B. Accrued and prepaid items
    - 1. Accrued items = buyer credit and seller debit
    - 2. Prepaid items = seller credit and buyer debit
  - C. General rules for calculating prorations
    - 1. The yearly charge is divided by a 360-day year (commonly called a banking year)

- or twelve months of 30 days each.
- 2. The yearly charge is divided by 365 (366 in a leap year) to determine the daily charge; then the actual number of days in the proration period is determined; and this number is multiplied by the daily charge.
- 3. The final figure will vary depending on the method used and the number of decimal places to which the division is carried.
- 4. Guidelines
  - a) In most states, the seller owns the property on the day of closing and prorations are made to and including that date.
  - b) Prorations are computed using a 30-day month and a 360-day year or using the actual number of days in the month in a 365 day year (refer to area practices).
  - c) Accrued real estate taxes are usually prorated; special assessments for public improvements are not.
  - d) Rents are usually prorated based on the actual number of days in the month of closing.
  - e) Security deposits belong to the tenants and must be transferred intact from the seller to the buyer.
- 5. Real estate taxes
  - a) If they are paid in advance, the seller should be reimbursed for the portion of the year remaining after the buyer takes ownership.
  - b) If they are paid in arrears, the buyer is credited for the time the seller was occupying the property.
- 6. Mortgage loan interest—usually paid in arrears

## SESSION FIVE

### REAL ESTATE APPRAISAL

- I. An appraisal is an estimate or opinion of value.
  - A. An appraisal can only be made as of a past or present time.  
(Effective Age compared to Chronological Age)
  - B. A CMA (competitive market analysis prepared by agent) is not an appraisal.
- II. Value is the present worth of future benefits arising from the ownership of real property.
  - A. Characteristics of Value ("DUST"):
    - 1. Demand
    - 2. Utility
    - 3. Scarcity
    - 4. Transferability
  - B. **Market value** is the most probable price a property will bring in an open and competitive market.
    - 1. The market must be truly open and competitive to establish value.
      - a. No undue pressure on either buyer or seller.
      - b. Both buyer and seller must be well informed.
      - c. A reasonable length of time must be allowed for the property to be exposed in the open market.

- d. The purchase must be made in cash or its equivalent.
- C. Market Value versus Market Price
  - 1. Market Value is an estimate based on the analysis of comparable sales and other pertinent market data (surveys entire market).
  - 2. Market Price - the sales price of a single property.
- D. The basic principles of Value (Economic Principles).
  - 1. **Highest and Best Use** - the use to which a property can be put which will return the greatest net income (profit).
    - a. Considerations in determining the highest and best use for a property:
      - (1) Legal uses only.
      - (2) Present use and the uses of nearby properties.
      - (3) Uses adaptable in the foreseeable future.
  - 2. Substitution - the value of property tends to be set by the cost of purchasing an equally desirable replacement. Use "comparable" property to estimate value.
  - 3. **Supply and Demand** - the value of property depends on the interaction between the demand for the property and the supply available.
  - 4. Balance - achieved when adding improvements to the land and structures will increase the property value.
  - 5. Conformity - to attain the highest value, properties should conform to existing neighborhood standards.
  - 6. Regression and progression - property of a lower value adversely affects the value of a better property in proximity, and vice versa.
  - 7. Anticipation - value can increase or decrease if one anticipates some future benefit or detriment from the property.
  - 8. Plottage (assemblage) - the merging of adjacent lots into one large lot with a higher value than the individual lots value separately.
  - 9. Diminishing Returns (increasing and decreasing returns) - a point at which improvements to land and/or structure will no longer have a positive effect on property value.
  - 10. **Contribution** - the value of any component of a property is what its addition contributes to the value of the whole or what its absence detracts from the value of the whole.
  - 11. Competition - excess profits tend to attract competition.
  - 12. Change - no physical or economic condition remains constant.

### III. The Three Approaches to Value

- A. The Sales Comparison Approach (**Market Data Approach** or Substitution Method).
  - 1. An estimate of value obtained by comparing the subject property with recently sold comparable (substitute) properties.
    - a. The selling price of comparables must be adjusted for any features dissimilar to the subject property.
    - b. There are four (4) principal factors for which adjustments to the comparable properties are made:
      - (1) Sales or financing concessions;
      - (2) Location;
      - (3) Physical features or amenities; and
      - (4) Date of sale.
    - c. The more numerous the adjustments that must be made between the

subject property and the comparables, the less accurate the estimate of value will be.

- d. A minimum of three (3) comparables is usually required to give a fairly accurate indication of value.
- e. Simplicity is the biggest advantage of the market data approach. No deductions must be made for physical depreciation of the property.
- f. The main disadvantages are that sometimes there are few comparables, and that the technique doesn't consider short term market fluctuations.
- g. The Market Data Approach is considered to be the most accurate appraisal approach because it bases its estimate on the market.
- h. It's the most common appraisal technique and the one considered best for single family dwellings.

**B. The Cost Approach (Summation Method or Reproduction Cost Approach).**

1. Based on the theory that value is set by the cost of reproducing a substitute property.
2. Steps in the Cost Approach:
  - a. Estimate value of the land as if vacant.
  - b. Estimate the cost of reproducing the buildings new.
  - c. Estimate the depreciation accrued by the subject property.
  - d. Subtract the depreciation from the cost of reproducing the buildings and add this figure to the value of the land.
  - e. The advantages of the summation method are that it establishes the upper limit of value, and that can be used for special purpose properties.
3. Reproduction cost versus Replacement cost.
  - a. Reproduction cost - the cost of exactly duplicating the subject property.
  - b. Replacement cost - the cost of acquiring a substitute property capable of satisfying the same use requirements of the subject property.
4. Depreciation - any condition that adversely affects the value of an improvement to real property.
  - a. Physical depreciation - the normal wear and tear on an improvement.
    - (1) Caused by factors internal to the property; such as the passage of time, the elements, rodents, delayed maintenance, negligent care
    - (2) May be curable or incurable depending on the cost of labor and materials.
  - b. Functional obsolescence - caused by internal factors that make the property less functional.
    - (1) Can be curable or incurable depending on economic feasibility.
    - (2) Can exist in new as well as old buildings.
  - c. Economic Depreciation - caused by factors that are external to the property.
    - (1) Because economic depreciation is caused by external factors, it is beyond the owner's control and is incurable.
    - (2) Some of the causes of economic obsolescence are: zoning changes, employment problems, increase in area crime rate, etc.
    - (3) Commercial and residential properties may be affected differently.
  - d. Depreciation is usually calculated on a straight-line basis.

**C. The Income Capitalization Approach.**

1. Based on the theory that the value of an investment is set by the ability of that investment to produce net income (profit).

2. Steps in the Capitalization Approach:
  - a. Estimate the annual potential gross income.
  - b. Subtract for vacancies and collection losses to obtain the "effective gross income".
  - c. Deduct the annual operating expenses from the effective gross income to obtain the net income (profit) (NOI – net operating income).
    - (1) Operating expenses are usually the taxes, insurance and maintenance.
    - (2) Does not include debt service, used in calculating cash flow.
  - d. Determine the capitalization rate by dividing the net operating income of similar properties by the sales price of those properties.
  - e. Obtain the estimated value of the property by dividing the net operating income of the subject property by the cap rate.
3. Compare: **Gross Rent Multiplier** - a type of market data approach where rental properties are valued based on the selling price of comparable rental properties and the gross rental income of those comparables.
  - a. The selling price of a comparable rental property divided by its gross monthly rent establishes its gross rent multiplier.
  - b. Could be divided by its gross annual rent to arrive at an annual multiplier.
- D. **Reconciliation** (correlation) - obtaining the final value estimate.
  1. All three (3) methods of appraising (market, cost and income) should be employed, if possible, to give the best indication of value.
  2. The values produced by the different appraisal methods should be weighed or balanced- not averaged.
  3. Appraiser will explain choices made and reasons for choices.

#### IV. The Appraisal Process

- A. Define the purpose and date of the appraisal.
- B. Gather, record and verify the necessary data.
- C. Use as many of the appraisal techniques as possible.
- D. Reconcile the estimated values for the final value estimate.

### PROPERTY MANAGEMENT

- I. Nature of business: Property manager may wear many hats from analyzing the market, marketing the property, salesperson, accounting and maintenance of property.
  - A. Three goals of property manager are: (1) achieve goals of owner, (2) generate income for the owner and (3) preserve and increase value of property.
  - B. Responsibilities:
    1. Budgeting and controlling expenses
    2. Keeping proper accounts with periodic reports to owner
    3. Maintain property and enhance owner's capital investment
    4. Contract with owners; often become general agents of owners; vary with size of project and owner's needs
    5. Examples of where property management occurs
      - a. Condominium associations

- b. Commercial buildings with many tenants
- c. Elderly housing
- d. Manufactured home parks
- e. Owners with multiple units

II. Management Agreement – Describes property, term of agreement, and defines management duties including authority, reporting (financial and otherwise), compensation, expectations of owner

### III. Types of Financial Reports

- A. Operating Budget - projects income and expenses for one year
- B. Cash Flow Report - details financial status of property
- C. Income - gross rentals and other income – may show adjustment for losses
- D. Expenses – shows fixed and variable expenses
  - Note: Cash Flow formula: NOI minus debt service
- E. Profit and Loss - financial picture of revenues and expenses to determine break even, gain or loss
- F. Budget Comparison Statement – compare budget with actual

### IV. Rental Rates/Leases

- A. Residential are monthly rate per unit
- B. Commercial usually stated as annual or monthly rate per square foot
- C. Market health is often the deciding factor of rates.
- D. Supply and demand, condition and location of property also affect the rates.

### V. Selecting Tenants – Collecting Rents – Maintaining Good Relations with Tenants

#### VI. Types of Maintenance

- A. Preventive—prevents problems and expenses
- B. Corrective—corrects problems after they occur
- C. Constructive—making property meet tenants’ needs (fit up)
  - 1. Tenant improvements – manage for compliance with law – owner’s standards
  - 2. Distinguish trade fixtures from regular fixtures
  - 3. Establish what will become the property of the Landlord

#### VII. Federal Laws Affecting Property Management

- A. American Disabilities Act (ADA) Title I and III
  - 1. Assess compliance with accessibility requirements
  - 2. Prepare retrofitting plan to bring into compliance
- B. Equal Credit Opportunity Act (ECOA)
  - 1. Use same lease application for every prospective tenant
  - 2. Requirement of credit report must be applied consistently
- C. Federal Fair Housing Act

#### VIII. Risk Management Techniques

- A. Security of tenants—must protect tenants from physical harm by intruders
- B. Building security—locks, windows, common entrances
- C. Criminal activity—grounds for eviction

- D. Avoid risk by removing sources—swimming pool example
- E. Control risk by preparing for emergency before it happens—fire doors, fencing
- F. Transfer risk by shifting the risk onto another party (insurance company)
- G. Retain risk by deciding that the chances of the event occurring are too small to justify the expense of any other response (take out insurance with large deductible)

#### IX. Types of Insurance

- A. Tenants—rental insurance HO-4 protects their belongings
- B. Commercial—Audit important by agent familiar with type of property
- C. Common Types of Coverage
  - 1. Fire and hazard—fire, wind, hail, water and smoke
  - 2. Flood—always separate policy
  - 3. Consequential loss, use, occupancy loss of rent or business interruption
  - 4. Contents and personal property
  - 5. Liability—covers risks owner assumes where public enters building
  - 6. Worker’s Comp—state laws require this when injuries are sustained by employees hurt in course of employment
  - 7. Casualty—theft, burglary, vandalism, health, accident insurance
  - 8. Surety bonds—cover owner against financial losses resulting from employee’s criminal act or negligence while performing assigned duties
  - 9. Multiperil for apartment buildings insurance package fire, hazard, public liability, casualty
  - 10. Condominium Insurance
- D. Claims—methods of determining claims
  - 1. Depreciated or cash value—cost of repairs less depreciation
  - 2. Current replacement cost—more expensive but more protective of property

#### X. Environmental Disclosures

- A. Lead based paint – perform audits, provide disclosures, hire trained workers
- B. Asbestos—older buildings
- C. Mold—increasing concerns and public awareness
- D. Radon—if tested.

### CONTROL OF LAND USE

- I. **Police Power** is the basis of the government's authority to create laws and regulations necessary to protect the public health, safety, and welfare.
  - A. Some of the uses of police power include zoning ordinances, building codes and subdivision regulations.
  - B. Police power does not require just compensation (compare eminent domain which does)
  - C. For review of eminent domain see Class #3, Transfer of Title, Part II Involuntary Alienation.
  
- II. **Enabling laws** of the state allow counties, towns and cities to control privately-owned real estate through:
  - A. Planning, Zoning, Subdivision, Building Codes, Environmental Protection, Design
  - B. Enabling laws constitute a delegation of authority from state to local municipalities

- III. Planning - master plans are devised by local communities to guide future growth and development.
  - A. A community must adopt a master plan prior to initiating zoning regulations.
  - B. In most states a plan is good for 5 years and then must be renewed. Zoning amendments cannot occur while the plan is stale.
  
- IV. Zoning ordinances are local laws that regulate and control the use of land and buildings.
  - A. Zoning applications include:
    - 1. Classification of land uses into residential, commercial, industrial, agricultural, and/or community
    - 2. The location and use of buildings (includes setbacks, buffer zones, permitted and conditional uses).
    - 3. Size, height, and the number of stories of buildings.
    - 4. Lot sizes.
  - B. Non-conforming uses
    - 1. Grandfathered use - a use of property established before zoning was enacted and permitted to continue even though it does not conform to the new law.
    - 2. Variance - permitted violation of a zoning ordinance (special exceptions)
  - C. **Spot Zoning** - zoning reclassification of a small area allowing a use not in conformance with the zoning of the surrounding area.
  - D. **Planned Unit Development (PUD)** - a land development combining several diverse land uses in one comprehensive plan.
  - E. **Inverse condemnation** – a constitutional action brought by property owner seeking compensation for land essentially “taken” by application of zoning regulations rather than eminent domain proceedings.
  
- V. Subdivision Regulations - Control the use of raw land.
  - A. Generally provide for street, road and highway specifications, water mains and sewer installation, easements for utilities, lot sizes, areas to be dedicated for public use.
  - B. Generally under jurisdiction of a planning board or commission.
  
- VI. Building Codes establish minimum standards for the construction, remodeling, maintenance and demolition of structures.
  - A. Require building permits and periodic construction inspections.
  - B. Require Certificates of Occupancy to indicate compliance with building codes.
  - C. Buyer or seller should agree in the sales contract which party will assume full responsibility for code violations.
  - D. Code violations may constitute consumer fraud in real estate transactions.
  
- VII. Environmental Protection Legislation
  - A. There are both Federal and State laws which have been enacted to protect the environment (example includes the Federal Clean Water Act).
  - B. See Chapter 21 on Environmental Issues for more details.
  
- VIII. Private Land Use Controls
  - A. **Deed Restrictions** (restrictive covenants) – limitations placed on use of a property by the owner, and binding on future grantees.
    - 1. To be valid and enforceable, such restrictions cannot be against public policy.

2. If conflicts with local zoning, the more restrictive of the two takes precedence.
  3. Injunctions are usually used to enforce deed restrictions.
  4. Private deed restrictions may be removed by a deed signed by the necessary parties (owners of the dominant tenement) (usually by Quitclaim Deed).
  5. **Doctrine of laches:** a delay in enforcement may result in loss of right to enforce.
- B. Developer created restrictions (covenants, conditions, and restrictions) (CC&Rs) are created by a declaration and often made part of the development permit.
  - C. Various private remedies: actions to prevent nuisances, the committing of waste and to evict trespassers.
- IX. Real Property Taxes are based on the value of the real property (*ad valorem*) and are used to pay for local services.
- A. If real property taxes aren't paid, the taxing jurisdiction can place a tax lien on the property. A real property tax lien can be enforced by a tax sale.
  - B. Real property tax liens generally take priority over all other liens.
  - C. An assessment is the town or city's valuation of the property for tax purposes.
  - D. Formula for calculating taxes: Assessed Value x Tax Rate = Tax
- X. Special Assessments - are special taxes levied on real estate to pay for improvements made by the taxing jurisdiction that benefit the property owner and make the property more valuable. Examples include sidewalks, sewer connections, water.
- XI. Escheat - property will escheat (revert) to the state, if the owner dies intestate (without a will) and there are no heirs; or if the property is abandoned and no proper claim is made.
- XII. Floodplains and Wetlands are generally protected under federal, state and local controls which restrict building and/or require zoning for conservation.
- XIII. Shoreline Protection - generally zoning laws affecting shorelines reflect environmental concerns, such as:
- A. Dredging restrictions on land within a given distance of navigable waters.
  - B. Filling and grading controls.
  - C. Tree-cutting rules.
  - D. Minimum lot sizes.
  - E. Standards for water supply and waste disposal.
  - F. Setback requirements for structures.
  - G. Subdivision regulations.

### ENVIRONMENTAL ISSUES

- I. Real estate brokers and salespeople must be very aware of how pollution and environmental risks have impacted real estate sales and values.
  - A. Consumers are much more aware of environmental risks today. (Eg. "green buyers")
  - B. If an agent suspects the presence of pollution on the property, s/he must make disclosure to both the client and the customer.
  - C. Because of the health risks and the extremely high costs of cleaning up pollution, its presence would be considered a material defect.
  - D. An agent should ask clients about the possibility of hazardous substances affecting the listed property; understanding that both him/herself and the client could be legally liable should pollution be discovered later.

## II. Hazardous Substances of Concern

- A. Radon Gas - an odorless radio-active gas produced by the decay of other radio-active materials in rock.
  - 1. Enters buildings from the ground through cracks in foundations or through floor drains.
  - 2. Long-term exposure to concentrations of radon gas which build up in a house can cause lung cancer.
  - 3. The U.S. Environmental Protection Agency has established unsafe levels of radon. Tests have been developed to monitor the levels in a home.
  - 4. Radon gas is dangerous only at concentrated levels; proper ventilation can reduce the amount of gas to safe levels.
  - 5. If a property is found to have radon gas, the seller is often obligated to find a way to eliminate the hazard.
  - 6. Whether the danger is real or only perceived, the presence of radon gas can lower the value of a home by at least the cost of eliminating the hazard.
- B. Asbestos - a mineral that was used for many years as insulation on plumbing pipes and heat ducts, as well as floor tile and roofing material.
  - 1. If left undisturbed, asbestos insulation is relatively harmless - dust particles released when the insulation is removed, or when it becomes old and begins to disintegrate are very dangerous to breathe.
  - 2. Approaches to eliminating the asbestos problem.
    - a) Leave the asbestos undisturbed.
    - b) Remove the asbestos.
    - c) Encapsulate the asbestos to contain the dust.
- C. Urea Formaldehyde Foam Insulation (UFFI) - man-made plastic foam that is pumped into the walls of buildings and acts as insulation.
  - 1. Can release gasses that have been found to cause many health problems, from cancer to headaches.
  - 2. Total removal of the insulation is the only way to eliminate the problem.
- D. Lead - a metal used in paint and plumbing because it can impede water flow.
  - 1. It becomes a health hazard when ingested - impairing mental and physical development in children, and causing high blood pressure in adults.
  - 2. Lead poisoning comes from two main sources.
    - a) Peeling or flaking paint eaten by children.
    - b) Plumbing systems.
- E. Waste Disposal Sites
  - 1. A landfill is a site that has been excavated and lined with a clay or synthetic liner to prevent the leakage of waste into the water system.
  - 2. Landfills at improper locations and improperly managed sites have caused major damage by leaking into waste supply.
  - 3. Despite heavy regulation by state and federal authorities, the proximity of waste disposal sites is a consumer issue, and agents should be aware of local sites.
- F. Underground Storage Tanks - an estimated three (3) to five (5) million tanks designed to hold dangerous substances, such as gasoline, exist in the U.S.
  - 1. The tanks are considered dangerous because they can rust and leak toxic material into the soil and groundwater.
  - 2. Federal law calls for the removal of the tanks and the disposal of both the tanks and polluted soil in a hazardous waste facility.

3. The two (2) major sources of pollution are:
  - a) Older gas stations with rusting tanks.
  - b) Older homes with underground fuel oil tanks.
- G. Groundwater contamination - groundwater includes both runoff at ground level and underground water systems that are sources of wells.
  1. Sources of contamination:
    - a) Waste disposal sites.
    - b) Underground storage tanks.
    - c) Pesticides and herbicides.
  2. Heavy government regulation is considered to be the only real protection against water contamination.
- H. Federal Environmental Legislation
  1. Resource Conservation and Recovery Act (RCRA) of 1976 - created to regulate generation, transportation, storage, use, treatment, disposal, and cleanup of hazardous waste.
  2. The Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA).
    - a) Superfund created to clean up uncontrolled hazardous waste dumps and to respond to spills.
    - b) Established a process for identifying liable parties and ordering them to take responsibility for clean up.
    - c) Administered through the Environmental Protection Agency, who has the authority to initiate clean-up work and assign liability to the persons it feels are responsible.
    - d) Liability under the Super Fund is considered to be strict, joint and several, and retroactive.
      - 1) Strict Liability - the owner is responsible to the injured party without excuse.
      - 2) Joint and Several Liability - each of the individual owners is responsible for the damages in whole.
      - 3) The Super Fund can assign retroactive liability to people who have owned the property in the past, as well as to the current owner(s).
      - 4) All owners and transporters of hazardous waste are liable for cleanup costs without regard to fault.
  3. Underground storage tanks - are regulated under the Leaking Underground Storage Tanks regulations (LUST) of 1984.
    - a) Governs installation, maintenance, monitoring, and failure of underground storage tanks.
    - b) The focus of this regulation is to protect groundwater in the U.S.
    - c) LUST places the financial responsibility on the tank owner.
  4. Super Fund Amendments and Re-authorization Act (SARA) 1986. (Text p. 388)
    - a) Established stronger clean-up standards for contaminated sites.
    - b) Increased the funding of the Super Fund.
    - c) Created the "innocent landowner immunity" concept.
  5. Common Law (case law) - provide a backdrop for the situations that don't fall specifically within state or federal law.
    - a) Offers an important remedy for damages for personal injury or property damage not covered under legislation.
    - b) Examples include nuisance, trespass

# SESSION SIX

## **FAIR HOUSING AND ETHICAL PRACTICES; EQUAL CREDIT OPPORTUNITY**

- I. Federal Fair Housing Laws include the Civil Rights Act of 1866, the Civil Rights Act of 1964, the Civil Rights Act of 1968 (Federal Fair Housing Act), Title VIII of the Civil Rights Act of 1968 as amended in 1974 and the Fair Housing Amendments Act of 1988. Together they prohibit discrimination in housing based upon:
- Race, Color, Creed (religion), National Origin, Sex (1974), Mental and/or Physical Handicap (1988), Familial status (families with children) (1988)**  
**THE ABOVE GROUPS ARE TERMED “PROTECTED CLASSES”**
- A. Civil Rights Act of 1866 prohibited discrimination based upon **race** for both real and personal property transactions.
1. Civil Rights Act of 1964 prohibits discrimination in any housing that is federally funded.
- B. Title VIII, Civil Rights Act of 1968 known as the Federal Fair Housing Act prohibits discrimination in private and public housing based upon **Race, Color, Creed** (religion), and **National Origin**.
- C. Civil Rights Act of 1866 as interpreted in case of Jones vs. Mayer outlaws all racial discrimination in real estate and real estate leasing.

Please Note: Both NH and VT state laws against discrimination in housing are more inclusive than the Federal Laws, including additional protected classes. Sexual orientation, age, and marital status are protected by both states. VT also protects gender identity and source of income.

- II. The following discriminatory acts are prohibited:
- A. Refusing to sell, rent or negotiate with any person, or **otherwise making a dwelling unavailable** to any person. (Consider effect of development on affordable housing.)
- B. Changing terms, conditions or services for different individuals as a means of discrimination.
- C. Using discriminatory advertising to restrict the sale or rental of residential property. Advertising can be directed toward a specific group if not discriminatory.
- D. Misrepresenting the unavailability of housing. Steering is prohibited.
- E. Making a profit by inducing an owner to list or sell her property because of the entry into the neighborhood of a person of a particular race, color, creed, national origin, etc. Blockbusting/Panic Peddling is prohibited.
- F. Discrimination in financing.
1. Includes altering the terms or conditions of a loan as a means of discrimination.
2. Redlining is prohibited if practiced for discriminatory reasons.
3. Refusing to sell, rent, or loan money purely because of economic reasons is permissible.
- G. Discrimination in brokerage services such as participation in M.L.S.& Realtors
- III. Exceptions to the Federal Fair Housing Laws (these are situations where the federal laws allow discrimination, even against people in the protected groups):
- A. Exceptions in the sale or rental of single-family residences:
1. Owner must be a private individual.
2. S/he can own no more than three (3) such homes.

3. The owner must be either the buildings' most recent occupant, 'r there cannot have been a transaction involving the property within 24 months.
  4. No discriminatory advertising used.
  5. No real estate broker used.
- B. Exceptions in the rental of multi-unit dwellings:
1. Owner must be a private individual.
  2. Four or fewer units in the building.
  3. One unit must be owner-occupied.
  4. No discriminatory advertising or real estate brokerage services used.
- C. Religious organizations may restrict the sale or rental of dwelling units they own based on religion only.
- D. Private clubs may discriminate in the rental or occupancy of property that they own based on membership only. Please Note: These exceptions do not apply to discrimination based on race; because of the Civil Rights Act of 1866 which prohibits discrimination based on race with no exceptions.
- E. An exception allowing discrimination against families with children under the age of 18 (familial status) is allowed if:
1. The unit is located in a complex designated as elderly housing for people 62 years of age, or older, or ...
  2. The unit is located in a complex where 80% of the units are occupied by at least one person aged 55 or older and the facility has a written policy to market to these age groups.
- F. Drug abusers and those who pose a threat to the health or safety of others are not protected by Federal law prohibiting discrimination based on mental or physical handicaps.
- IV. Enforcement - Any person may file a complaint with HUD within one year; or has two (2) years to bring an action directly in a Federal or state court. The burden to prove that discrimination exists as always on the complainant. The maximum penalty for first violation is \$16,000. To help defend against claims of discrimination, some trade associations recommend keeping Prospect Equal Service Reports.
- V. Equal Housing Opportunity Posters must be displayed in broker's offices, model homes, 'lender's offices, etc. or ***prima facie*** evidence of discrimination will be held to exist.
- VI. The Federal Equal Credit Opportunity Act expands the number of classes protected from discrimination in financing to include age, marital status, or source of income; and requires that all rejected credit applicants be informed, in writing, of the reasons for credit denial.

### **REAL ESTATE INVESTMENT – TAX BENEFITS**

- I. Review tax benefits and deductions. Text pgs. 35-36 (home) and 434-436 (investment)
- II. Review highlights of Chapter 23 of Text pgs. 429-439.
  - A. Advantages and disadvantages of real estate investment. Pg. 431
  - B. Cash flow analysis. Pgs. 432-433
  - C. Leverage, Equity Buildup and Pyramiding. Pgs. 433-434.
  - D. Syndicates and REIT's. Pg. 437

## PROPERTY DESCRIPTION

Contracts, especially contracts that act to convey any interest in real property, must exactly describe the property being conveyed. There are three (3) basic ways to legally describe real property.

### I. The Metes and Bounds description.

- A. Earliest type of legal description.
- B. Description begins at a specific "point of beginning" (P.O.B.), and by reference to linear measurements and directions, proceeds around the boundaries of the tract.
- C. To insure that the tract of land being described is completely enclosed, the metes and bounds description always ends at the P.O.B.
- D. The property lines of a tract are defined by the linear distance between fixed markers or monuments. Monuments may be natural (trees, rivers, etc.) or artificial (cement markers, iron stakes, etc.).

### II. Rectangular Survey System (Government Survey System).

- A. Property description is based on a grid system of north-south and east-west parallel lines.
- B. Not used in most eastern seaboard states.
- C. Each township is 36 square miles and each section of the township is 1 square mile or 640 acres. Study how to locate and how to calculate acreage.

### III. Lot and Block System (Plat).

- A. In this system, a survey Plat map is drawn by a licensed land surveyor and recorded at the registry of deeds.
- B. The map is very complete, and includes the name of the developer, the name of the surveyor, the date the subdivision was approved, etc. as well as the lot and block numbers of the parcel being described.
- C. The description of the property in the P & S Agreement, the deed, etc., is made by referring interested persons to the map in the land records.
- D. The easements and rights depicted on the survey usually apply to all property shown.

IV. A final method of describing property - using the street address or tax map number- is considered too inaccurate to be used as an effective legal description.

## REAL ESTATE MATH

### Compensation, Commission & Fee Questions

1. At closing, the seller paid the broker \$22,000 which was equivalent to 6 percent of the selling price. What was the selling price of the property?
2. Joe listed his property with Maple Realty that charges a flat fee of \$3,000 regardless of who sells the property. The agreement provides that if an agent from another company brings the buyer that purchases the property, the owner agreed to pay that company a 3 percent commission. An agent from another company found a buyer for the purchase price of \$200,000. If a contract is formed, what is the total commission that the owner will pay?
3. Owners sold property and paid a commission of 6 percent. The check after commission was \$470,000. What was the selling price of the property?

### Valuation/ Market Sale Price and Yields

1. Last year an apartment building had an effective gross income of \$55,000 and operating expenses of \$5,000. If the rate of return is 10% what is the value of the apartment building?
2. Two years ago a buyer paid \$140,000 for a house. The property has depreciated 3 percent each year for the past two years. What is the value of the property today?
3. If the gross rent multiplier of a property is 110 and the total rent is \$1,500 monthly, what is the value of the property?

### Tax and Other Prorations

1. The market value of a property is \$235,000, it is assessed at 50%, and the tax rate is \$5.50 per \$100. What are the monthly property taxes?
2. A seller renewed and prepaid her one-year insurance policy costing \$1,200 on September 1, 2011, and sold the property with the buyer assuming her policy on January 15, 2012. How much will be credited to the seller on the closing statement?

### Net to Seller, Cost to Buyer

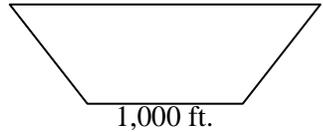
1. Semiannual property taxes of \$450 were paid only for the first half of the year. The property sold on July 15. What entries would be included on the settlement statement?
2. The buyer had a 20 percent down payment on a property she purchased for \$100,000. She is required to pay a 1 percent origination fee, \$500 for title insurance, \$600 for attorney fees, and one discount point. How much money will the buyer owe at the closing?

### Amortization, Points, Prepayment, and Loan-to-Value

1. A property was purchased for \$210,000. If the loan was \$168,000, what was the loan-to-value ratio?
2. A lender charged three discount points on a \$70,000 loan. What was the cash outflow of the lender?
3. The semi-annual interest paid on a loan was \$6,875. If the interest rate is 5.5 percent, what was the loan amount?
4. A bank agreed to loan \$60,000 at 6 percent interest for 30 years and charged 3 points to negotiate the loan. What was the effective yield to the lender?
5. One lender charges 6.5 percent interest and the second lender charges 7 percent interest. How much money will the borrower save the first year on a \$150,000 term loan if he goes with the first lender?
6. The buyers borrowed \$60,000 at 4 percent for 30 years. Their monthly payment is \$286.45. How much of their first payment will be applied to the principal balance?

## Measurement

1. Using the dimensions in the following diagram, what is the approximate cost to purchase at \$6,000 per acre?  
1,400 ft.



Distance between parallel lines (depth) = 400 ft.

2. A two story home measures 25' by 50'. A one story family room was added that measures 20' by 20'. At a cost of \$9.95 per square yard for carpet and \$2 per square yard for installation, how much will it cost to carpet the house and family room?
3. The N1/2 of the SE1/4 of the SW1/4 of the S1/2 of Section 32 sold for \$5,000 an acre. What was the selling price?

## Property Management/Investment

1. A space leases for \$1,000 per month. The owner pays a property manager 10% of the gross income as commission. How much does the owner pay annually?
2. The lease agreement was as follows: \$1,300 fixed monthly plus 5% on all sales over \$800,000. If this year's gross sales are \$1,500,000, how much rent will be paid for this year?
3. In a 15 year graduated lease, tenant pays \$500 per month for the first five years, and a \$50 per month increase every five years thereafter. If the property manager receives a commission of 10% of the gross rents paid, what will be the total commission paid by the end of the term?