



**LOUISIANA
BROKER RESPONSIBILITIES
MANUAL**

GETTING STARTED IN THE REAL ESTATE BROKERAGE BUSINESS

OBJECTIVES

- Getting started in the Real Estate Brokerage business is about taking the right initial steps to ensure success. There are specific legal requirements to the business. It is crucial you understand these before you launch your Brokerage.
- This lesson is an introduction to the basic requirements of the Real Estate Brokerage business. Upon completion of this lesson, you should be able to:
 - Identify the different types of licensing required in Louisiana.
 - Understand the legal forms of business and the basic structure and requirements of each type.

Types of Louisiana Real Estate Licenses

In Louisiana, there are three types of licenses required to sell property in the state:

- Company License
- Sponsoring or qualifying broker license
- Salesperson License

Company License

- A legal business entity setup to actively market and sell property in the State of Louisiana must be licensed as a broker by the Louisiana Real Estate Commission (LREC).
- To obtain a Corporate, partnership, or limited liability company real estate broker's licenses, the following must be submitted:
 - Application with appropriate fee
 - Designation of a qualifying broker
 - Evidence affirming corporate or trade name

Sponsoring or Qualifying Broker License

- A sponsoring or qualifying broker must be licensed as a broker issued under current LREC requirements:
 - You must have been actively licensed as a real estate salesperson for at least four years in any state/jurisdiction.
 - You must have obtained a high school diploma or equivalency certificate (GED)
 - You must show proof of successful completion of one hundred fifty (150) classroom hours or its equivalent in courses specified and approved by the LREC.
 - You must comply with all application procedures required by the LREC. This includes the submission of a criminal background history.
 - You must pass the broker licensing examination.
 - You must provide proof of mandatory errors and omissions insurance prior to issuance of license.
- The LREC requires one hundred fifty (150) hours of pre-licensing education prior to issuance of a broker license.
- At its discretion the LREC may grant partial credit toward the broker pre-licensing educational requirement.
- The credit will be based on the date the course was completed and the applicability of the subject matter to current broker educational requirements.
- No substitution will be allowed for Real Estate 202, the thirty (30) hour course which covers the Louisiana Real Estate License Law, Commission Rules/Regulations, Law of Agency, and Civil Law pertaining to real estate.
- An additional thirty hours must be completed in Real Estate 203, Broker Responsibilities, or its equivalent. The remaining hours can be obtained in a review of real estate principles/practices or other real estate electives. Broker courses may be obtained through the following sources:
- Check with the LREC for acceptable course work from other jurisdictions which may be acceptable for credit.

Salesperson license

- Salespersons working under a licensed broker must also be licensed by the LREC. To be issued a real estate salesperson license one must meet the following requirements:
 - You must be at least 18 years of age.
 - You must have obtained a high school diploma or equivalency certificate (GED).
 - You must show proof of successful completion of ninety (90) hours of real estate education in courses approved by the LREC.
 - You must comply with all application procedures required by the LREC. This includes the submission of a criminal background history.
 - You must pass the real estate salesperson licensing examination.
 - You must be sponsored by a licensed real estate broker and provide proof of errors and omissions insurance prior to license issuance.
- The LREC requires ninety (90) hours of pre-licensing education prior to issuance of a real estate salesperson license.
- The LREC may grant partial credit toward the salesperson pre-licensing educational requirement for courses completed more than five years prior to the date of application
- Such credit will be based on the date of completion and the applicability of the subject matter to current educational requirements.
- Salesperson pre-licensing hours must be in specific real estate courses that include coverage of real estate principles/practices, the Louisiana Real Estate License Law, Commission Rules/Regulations, Law of Agency, and Civil Law pertaining to real estate.
- Courses may be obtained through State Certified Real Estate schools, Colleges and Universities and through Course work completed in other licensing jurisdictions.

Post-Licensing & Continuing Education Requirements

- The LREC has specific requirements for post-licensing and continuing education requirements for brokers and salespersons.
- The post-license education requirement states that the student must pass an examination on course content required for that license.
- Continuing education requires specific course-work be completed annually before a license can be renewed.

Applicants with license history from other states

- Broker or salesperson applicants with license history, past or current, from other states must comply with the following:
- Submit an official license history verification from the state/jurisdiction in which the license was issued which includes:
 - Applicant's complete name
 - Mailing address
 - Telephone number
 - Detailed history applicant's license
 - This history should include a list of all real estate education completed as well as any information regarding past or pending disciplinary action against the applicant.

Examination requirement

- Examination results from other jurisdictions may serve as a substitute for the National portion of the Louisiana examinations for both brokers and salespersons.
- The applicant must provide proof of passing an equivalent license examination within five years of the date of application for a license in Louisiana.
- If a waiver is granted, the applicant will be required to pass only the State portion of the Louisiana salesperson or broker license examination.

Criminal background check

- Since January 1, 2012, all persons applying for a real estate license must provide a criminal background history, as part of the initial application process.
- To ensure consistency in the background investigative process the LREC has contracted with a third party for the background history investigation.
- The applicant is required to initiate the background check process by setting up an account with the provider.
- Look for information about the current provider on the LREC website on how to initiate the process.

Legal Forms of Business

Introduction

When you decide to become a real estate broker you must first decide the form of business entity you are going to establish.

Are you going to be a?

- 1) Sole Proprietor
- 2) Corporation
- 3) Partnership
- 4) Limited Liability Corp. (LLC)
- 5) Or affiliate with a franchise

This decision will have long ranging impacts on matters of taxation, asset protection, accounting and many others. Consultation with a trusted business attorney and CPA will go a long way to making the right decision for your future business.

Sole proprietor

- The sole proprietorship (*a business entity owned by one person*) is the least expensive and easiest business entity to form.
- Termination of the entity may occur due to license expiration, inactive status, or death of a licensee.
- The sole proprietorship has a variety of advantages, including:
 - Ease of formation
 - A centralized management regime
 - No corporate tax
- The sole proprietorship also has a variety of significant disadvantages as well, including:
 - Unlimited liability
 - Limited business life
 - Difficulty of raising capital
- It can be difficult because any new capital is based on the ability of the sole proprietor to raise it. There is no stock that can be sold in a sole proprietorship.
- A sole proprietor must file Schedule C, Profit (or Loss) from a business or profession, with Form 1040 to the IRS. Estimated quarterly tax payments must be paid, as appropriate.

Corporation

- A corporation is a legal entity formed by filing articles of incorporation with the Secretary of State, who issues a charter.
- Corporations can be foreign or domestic.
- Domestic corporations are formed within the state; whereas, foreign corporations are created outside of the state.
- A corporation may issue stock to raise capital. Stockholders elect a board of directors that hires officers to manage the corporation.
- The stockholders must meet annually.
- Corporate management is typically centralized or controlled in a top down fashion. Officers must consist of a president, secretary and treasurer, although one person may fill all offices.
- The directors and the officers of the corporation have a fiduciary (a relationship of trust) relationship with the corporation.
- The biggest advantage of a corporation is the stockholders do not have liability for the company's business activities.
- Liabilities attach to the corporation, not personally to officers, directors or stockholders.
- One of the biggest disadvantage of a corporation is double taxation of profits.
- Not only does a corporation have to pay tax on its earnings, but its stockholders also have to pay tax on the dividends they receive.
- If the organization is setup as a Subchapter S Corporation, double taxation can be avoided.
- Corporate income flows for taxation through individuals (stockholders) at their tax rates.
- In order for a Subchapter S Corporation to exist, the corporation is limited to a maximum of 75 stockholders. All corporations must obtain a federal employer tax identification number and file appropriate tax returns.

Partnership

- General or limited partnerships are forms of business ownerships that may also be used to operate real estate brokerage firms.
- As with the corporation, partnerships may also procure a broker's license for their company, as long as the partnership has a qualifying broker.
- In a general partnership, all partners can participate in the daily management of the organization. Ownership may not be equal.
- There are a variety of disadvantages with a general partnership:
 - Transferability is difficult.
 - The partnership is dissolved in the event of death, bankruptcy, or withdrawal of any partner.
 - All partners are jointly and severally liable for all action.
- Another type of partnership is the limited partnership, created by filing a certificate of limited partnership with the Secretary of State.
- A copy must also be filed with the clerk of the circuit court in the county where the home office is located.
- In a limited partnership, there must be at least one limited partner and one general partner.
- The general partner carries the management responsibilities, and has extensive liability.
- The general partner in a limited partnership is held personally responsible for the debts of the partnership.
- Limited partners are only responsible to the extent of their investment.

Limited Liability Company (LLC)

- A limited liability company (LLC) is the United States-specific form of a private limited company.
- An LLC is a business structure combining the pass-through taxation of a partnership or sole proprietorship with the limited liability of a corporation.
- An LLC is not a corporation; it is a legal form of a company that provides limited liability to its owners in many jurisdictions.
- LLCs do not need to be organized for profit.
- LLCs are not a separate taxable entity. The owners of the LLC report business profits or losses on their personal income tax returns.

- Like their corporate counterparts, LLC owners are shielded from personal liability for debts incurred by the business and other claims. This is the “limited liability” feature of this type of business entity.
- Creditors usually can't reach the personal assets of LLC owners, such as their residence, vehicles or other personal property.

Franchise affiliation

- A franchise is typically a national or regional branded Real Estate Marketing and Sales organization. Local offices are affiliated through a franchise agreement.
- The franchisor grants the franchisee the right to use its trademark, logos, business systems, training services and other marketing and sales assistance agreed to in the franchise agreement.
- The franchisee usually pays a percentage of sales revenues on an ongoing basis in addition to any up-front fees.
- A franchise is typically a national or regional branded Real Estate Marketing and Sales organization. Local offices are affiliated through a franchise agreement.
- Advantages of a franchise include:
 - Name recognition
 - Marketing strength
 - Structured training programs
 - Technology optimization
 - Relocation services
 - Support network
- Some disadvantages of a franchise:
 - Large offices – more competition for the managing broker's time
 - Franchise fees and percentages
 - Dependent on strength of franchisor
 - Subject to franchise restrictions
- What should you look for in a franchise?
 - Market leader
 - Strong brand
 - Utilizes current technology
 - Strong social media presence
 - World-class training program
 - Leadership values
 - Growing brand

Other business considerations

- Brokers may have multiple offices throughout the state, provided they are appropriately licensed as branch offices.
- Licensing as a real estate broker is not sufficient to sell securities; additional licensing to sell securities is required by the Securities Exchange Commission and other licensing or regulatory entities.
- Vacancies for the qualifying broker's position must be filled within five (5) days.
- No brokerage business may be conducted without a principal broker unless approval is obtained.
- Upon dissolution of a company, all licenses must be returned within ten (10) days.

STRUCTURING YOUR REAL ESTATE BUSINESS

OBJECTIVES

To plan for success, it is crucial you structure your real estate business using proven models and methodologies. The identification and management of risk must be at the forefront of your planning and operational philosophy.

This lesson will take a brief look at the history and evolution of the Real Estate Brokerage business. We will look at business operations where you can reduce and manage risk.

Upon completion of this lesson, you should be able to:

1. Identify the different real estate broker models of operation.
2. Understand how to identify and manage different risk areas your brokerage will encounter.
3. Identify needed outside resources.

History and Evolution of Real Estate Brokerage

There are many different aspects of the Real Estate business of today.

- Residential and commercial sales
- Property development
- Property management
- Appraisal (and others)

But where did it all begin?

The real estate business reaches back to the earliest days of civilized man and beyond. In the days of the caveman, real estate acquisition occurred at the end of a big stick.

Rather than a property deed, title of ownership hinged on the strength of the tribe to hold it from other clans looking to “acquire” property.

Our ancestors abandoned the hunter-gatherer lifestyle gradually over several thousand years and began moving towards an agrarian society which ultimately heralded the advent of home ownership.

The young Grecian King, Alexander the Great, spent most of his reign engaged in—aggressive acquisition—throughout Asia and Northern Africa.

By the time the Alexander reached 30-years-old, he had amassed one of the largest real estate dynasties of the ancient world.

The conquered people of the lands, many of them no more than clans of farmers, paid homage to the king by feeding his armies. In essence it was one of the earliest examples of rent.

The United States got into real estate when it agreed to purchase the Louisiana territory from the French in 1803.

President Thomas Jefferson struck a deal with Napoleon to buy New Orleans and the west bank of the Mississippi River for \$10 million dollars. But then the French government offered -

for five million more they would sell all of the Louisiana territory. Thomas Jefferson approved the deal and used his constitutional power to sign treaties to buy the land.

This started the trend of government land treaties that stretched the property of the United States to the western shores of the continent by the middle of the 19th century.

The Industrial Revolution of the early 1800s brought with it a shift from an agricultural to a manufacturing society.

Every aspect of daily life was impacted by this transition, especially in the ways it affected housing and property ownership.

This period saw the rise of tract housing designed to meet the needs of the new manufacturing employers and their workforce.

In many ways this period saw the beginning of the separation of white collar and blue collar workers. From a real estate perspective the lower end of the class spectrum, the blue collar workers, were the renters of the time and dreamed of the day they could by their own home – The American Dream.

In 1855, Baird & Warner becomes the nation’s first full-time Real Estate broker and continues to do business throughout Chicago and the surrounding area.

According to Realtor.org, in 2012 there were over 86,000 real estate brokerage firms operating in the United States.

To manage the daily tasks of developing, marketing and selling real estate property is the primary function of today’s real estate broker and agents.

Historically, home ownership was the domain of royals and aristocrats.

Today the opportunity to own property is within reach of even people with modest means. It's the broker's job to bring together buyers and sellers.

Real Estate Brokerage – Traditional Model

In the traditional brokerage business model, a full-service agent who provides many services including: but not limited to....

- Marketing the property
 - Listing service
 - Advertising
 - Hosting open houses
- Reviewing contracts
- Finding property for buyers
- Negotiating – Offers/Counters
- Assisting with the closing

In our traditional brokerage model there will be one Louisiana state licensed real estate broker who is responsible for the operation of the brokerage including all salespersons operating under his license.

- In our example this broker also owns the agency.
- He provides the building.
- He contracts with one or more sales agents to engage in real estate marketing and selling activities.
- He may even provide some internal administrative support for the operation.

Pros	Cons
Sales team	Losing high producing agents
Knowledge sharing	Managing commission splits
Can manage overhead	Risk assumption
Pooled admin resources	Managing conflict
Can trim non-producers	Higher cost model
Market centric	Competitive pressure
Shared technology	

Real Estate Brokerage – Limited Service Model

A real estate broker who offers less than all the traditional brokerage services is known as a limited service broker.

Typically, the limited service broker provides sellers with listings on the local multiple listing service, and perhaps some advice and yard signs, in exchange for a flat fee that is fully earned whether the property sells or not.

Also known as Flat Fee MLS broker

Pros	Cons
Low cost structure	Competing against full service
Simple business plan	Low price structure
Highly marketable to FSBO	Needs high volume
Needs little admin support	
Seller access to MLS	

Real Estate Brokerage – Virtual Office Model

A highly successful real estate professional once said...

If you want to waste an hour of your day, stop by the office for five-minutes.

With proliferation of the internet, social media, webvertising and the costs associated with brick and mortar offices, many agents and brokers are moving to a home office – telecommuting.

A virtual office is much more than just staying home to work.

A successful virtual office is about having core technologies in place for real-time office operations.

It must:

- Be easy to use
- Include real-time chat
- Have easy file management
- Include real-time collaboration
- Integrate conferencing (*Video if possible*)

It doesn't always mean there won't be a brick and mortar building somewhere. The managing broker may have a small office somewhere as headquarters, but it's not always a requirement.

The point is – in the virtual world, your team should be able to work just as efficiently from their kitchen tables as they do from a central location.

Pros	Cons
Reduced cost	Less ability to supervise
More efficient	Dependent on network
Agents generally available	Technology driven
Better time management	Might not have central location
Reporting metrics	

Identify and Manage Risk

Risk is one factor every real estate broker faces every day and it comes in many forms:

- Errors and omissions
- Property and casualty
- Vehicles
- And more...

Errors and Omissions Insurance (E&O)

E&O insurance covers you or your company should you be held responsible for a service you provided, or failed to provide, to a client that failed to meet an expectation or whatever you agreed to provide.

It works much like your doctor's malpractice insurance.

Most E&O policies cover judgments, settlements and defense costs. Even if the allegations are found to be groundless, thousands of dollars may be needed to defend the lawsuit. They can bankrupt a smaller company or individual and have a lasting effect on the bottom line of larger companies.

Errors and omissions insurance is mandatory for all licensees per R.S. 37:1466.

Look for the example O&I insurance policy found in the resources folder.

Examples of E&O:

- Failure to properly maintain property resulting in property value decrease
- Commingling funds
- Failure to collect rents

- Wrongful eviction or discrimination
- Subcontractor negligence
- Security failures
- Conflict of interest

Property and Casualty Insurance

Property and casualty insurance is purchased to protect against property losses to your business, home or vehicle.

It also protects you from legal liability that may be a result of injury or damage to another's property.

This type of insurance can protect a person or someone else having an interest in the insured property.

Having a broad range of property and casualty insurance, in adequate amounts, is your front line of defense in mitigating risk.

Let's take a quick look at the different coverages to consider.

Commercial property insurance can protect your business assets from property losses due to:

- Fire
- Water damage (burst pipes)
- Storm damage
- Theft
- Vandalism

Property insurance protects many aspects of your business:

- Your property
- Your signs
- Fencing
- Equipment
- Any inventory

Casualty insurance is more about your liability when someone is injured in some way by the actions (or inactions) of you or another associated with your business.

This is usually in the form of some umbrella policy that covers a myriad of injuries that result in a law suit.

These might include, but not be limited to things like:

- Libel and slander
- Contract disputes
- Liabilities caused by misconduct

It is imperative that all independent sales agents contracted to the brokerage carry adequate automobile coverage for protection.

The agent's brokerage firm will almost always be named co-defendant in a vehicular lawsuit.

For this reason some brokers insist on being named co-insured and often will require their agents to carry excess liability coverage.

Insurance coverages for vehicles typically includes liability for?

- Personal injury
- Property damage
- Bodily injury liability

- Collision
- Uninsured motorist coverage

In addition to liability insurance brokers may require the agent to maintain comprehensive coverage to protect against:

- Theft
- Fire
- Natural disasters
- And more...

In summary, it is the managing broker's responsibility to put in place all forms of liability and property coverage in place to protect the business from risk.

Recruit outside advisors

Never underestimate the value of your outside advisors. The importance of good advice is easy to overlook.

You'll need:

- Attorney
- CPA
- Banker
- Insurance broker

Recruit outside advisors – Business Attorney

A small business attorney will be crucial as you navigate the legal complexities of small business ownership.

From the day you decide to open your brokerage to day you sell it, this is a relationship you must build on absolute trust.

A good business attorney will protect your personal and business interests in several areas.

What will you want to know about your small-business attorney?

1. Experience with real estate brokers?
2. Who will be handling your business?
3. Are there any client conflicts?
4. Cost and billing structure
5. Availability
6. References

Recruit outside advisors – CPA

A Certified Public Accountant is not simply a number-cruncher. A CPA will help you set your financial strategy in place that puts you on the path to success.

Some of the services a CPA will provide are:

- Financial planning
- Tax preparation
- Setting up accounting procedures
- Investment advice
- Estate planning

Some tips for finding the right CPA:

- Ask your attorney for a reference
- Ask other business leaders
- Look for CPA directory
- Ensure professional membership
- Look for three firms to compare

Once you have selected three firms to compare, ask these things:

- Years of experience
- Background
- Do they have a specialty
- Hours and availability
- Association affiliations
- References
- Other Real Estate brokers they may do accounting for.

You may not want to select a CPA that is already doing business with your closest competitor. They may not say but it doesn't hurt to ask.

Selecting the right CPA can have significant impact on your success so it's important to get it right.

After selecting your lawyer and CPA the next choice should be your banker.

The crucial attributes that should drive this decision are:

- Location and size
- Rates
- Experience
- Services
- Trust

Having a solid private banker in your corner is imperative. After all, your money is the life blood of your brokerage. A private banker can:

- Arrange credit lines
- Help with account management
- Consult with fluctuating rates
- Be a single point of contact
- Navigate financial difficulties

To round out your cast of consultants, a good insurance broker should be your next find.

Because of the various types, plans and prices in the insurance business you will want someone who can choose the best options and manage your coverage.

It's one less headache for you.

Trade Association Resources

There are trade associations that focus on the Real Estate sales industry.

Primary among these are:

- National Association of Realtors
- National Association of Real Estate Brokers

Membership in one of these organizations brings many benefits to the table including:

- Training resources
- Insurance referrals
- Marketing resources
- Transaction management
- Technology services

Prospective agents already holding memberships in one of these associations bring a bit of prestige and should hold advantage over non-association prospects.

PERSONNEL: HIRING, TRAINING, AND STAFFING

Your future success as a Real Estate Broker hinges primarily on the agents you bring into the brokerage. To sort through a pile of candidates and finding motivated salespeople may be the difference between success and failure.

This lesson will take a look at both federal and state employment laws. We will discuss, in practical terms, the Hiring and supervision of employees and independent contractors.

Upon completion of this lesson, you should be able to:

1. Understand the fundamentals of federal employment law.
2. Understand the basic tenants of Louisiana employment law.
3. Have a basic understanding of employee hiring and supervision tactics.

Employment Law - Federal

Federal employment laws are extensive. Deviation may bring heavy financial consequences.

For this discussion we will focus on the following:

- Fair Labor Standards Act (FLSA)
- The Occupational Health and Safety Act (OSHA)
- Worker's compensation
- Family and Medical Leave Act (FMLA)
- Equal Employment Opportunity
- Age Discrimination (ADEA)
- Americans w/Disabilities Act (ADA)

Fair Labor Standards Act (FLSA)

The FLSA is administered by the Wage and Hour Division. The act establishes standards affecting employees, both private sector and government positions.

We'll break it down to these core areas of regulation:

- Minimum wage
- Overtime
- Hours worked
- Recordkeeping
- Child labor

Independent contractors have slightly different requirements so we will discuss those separately from exempt and non-exempt employees.

Minimum wage

Federal minimum wage is \$7.25 per hour effective July 24, 2009.

Many states also have minimum wage laws. Some state laws provide greater employee protections; employers must comply with both.

Employers must pay the highest prevailing minimum. These standards affect more than 130 million workers, both full-time and part-time, in the private and public sectors..

Executive, administrative, professional and outside sales employees -(as defined in Department of Labor regulations) - and who are paid on a salary basis are exempt from the minimum wage provision of the FLSA.

Overtime

Employees covered by the FLSA, unless exempt, must receive overtime pay for hours worked over 40 in a workweek at a rate not less than time and one-half their regular rates of pay.

There is no limit in the Act on the number of hours employees aged sixteen (16) and older may work in any workweek.

Executive, administrative, professional and outside sales employees are also exempt from the FLSA overtime provision..

The Act does not require an employer to pay overtime for work on Saturdays, Sundays, holidays, or regular days of rest, unless such overtime is worked on those days.

The Act applies on a workweek basis. An employee's workweek is a fixed and regularly recurring period of 168 hours — seven consecutive 24-hour periods.

This need not coincide with the calendar week, but may begin on any day and at any hour of the day. Different workweeks may be established for different employees or groups of employees. Averaging of hours over two or more weeks is not permitted. Normally, overtime pay earned in a particular workweek must be paid on the regular pay day for the pay period in which the wages were earned.

Hours Worked

By statutory definition the term "employ" includes "to suffer or permit to work."

Hours worked includes all the time an employee is required to be on the employer's premises or workplace, and on duty.

"Workday", in general, means the period between the time on any particular day when such employee commences his/her "principal activity" and the time on that day at which he/she ceases such principal activity or activities. The workday may therefore be longer than the employee's scheduled hours.

Any additional hours worked outside the employees scheduled time, for example, to finish assigned tasks are considered compensable time and must be paid.

Depending on the circumstances "waiting time" may be considered compensable.

Generally, the facts may show that the employee was engaged to wait (which is work time) or the facts may show that the employee was waiting to be engaged (which is not work time).

For example, a secretary who reads a book while waiting for dictation or a fireman who plays checkers while waiting for an alarm is working during such periods of inactivity. They have been "engaged to wait."

An employee who is required to remain on call at home, or who is allowed to leave a message where he/she can be reached, is not working (in most cases) while on call.

Additional constraints on the employee's freedom could require this time to be compensated.

Rest periods of short duration, usually 20 minutes or less, are common in industry and are customarily paid for as working time.

Unauthorized extensions of authorized work breaks need not be counted as hours worked when the employer has expressly and clearly communicated to the employee that the authorized break may only last for a specific length of time and that any extension of the break is contrary to the employer's rules, and any extension of the break will be punished.

Bona fide meal periods (typically 30 minutes or more) generally need not be compensated as work time.

For other activities that may be considered compensable, such as travel, lectures, meetings or training refer to the Wage and Hours Division guidelines.

Recordkeeping

Every covered employer must keep certain records for each non-exempt worker.

The Act requires no particular form, but does require the records have specific identifying employee information and associated hour/wage data.

At a minimum the personnel data to maintain must include:

1. Employee's full name and social security number
2. Address, including zip code
3. Birth date, if younger than 19
4. Sex and occupation
5. Time and day of week employee's workweek begins
6. Hours worked each day
7. Total hours worked each workweek
8. Basis on which employee's wages are paid (e.g., "\$9 per hour", "\$440 a week", "piecework")
9. Regular hourly pay rate.
10. Total daily or weekly straight-time earnings.
11. Total overtime earnings for the workweek.
12. All additions to or deductions from the employee's wages.
13. Total wages paid each pay period
14. Date of payment and the pay period covered by the payment

The employer shall preserve for at least three years any payroll records or collective bargaining agreements.

Wage calculation records should be retained for two years.

Things like time cards, wage rate tables, work and time schedules, and records of additions to or deductions from wages must be kept.

Child Labor

The FLSA has specific guidelines for hiring children under the age of 18.

There are no Federal rules about employing 16 or 17-year-olds, although there are restrictions on the types of jobs they can perform.

For an extensive explanation of the Federal child labor laws go to www.youthrules.dol.gov/

Occupational Safety & Health Act (OSH)

With the *Occupational Safety and Health Act of 1970*, the United States Congress created the Occupational Safety and Health Administration (OSHA).

The OSHA mission is to assure safe and healthful working conditions for employer personnel by setting and enforcing standards and by providing training, outreach, and education.

The core requirement under 29 USC 654:

- a) Each employer:
 - 1) Shall furnish to each of his employees employment and a place of employment which are free from recognized hazards that are causing or are likely to cause death or serious physical harm to his employees.
 - 2) Shall comply with occupational safety and health standards promulgated under this Act.
- b) Each employee shall comply with occupational safety and health standards and all rules, regulations, and orders issued pursuant to this Act which are applicable to his own actions and conduct.

For further OSHA regulations refer to: www.osha.gov

Worker's Compensation

The U.S. Department of Labor, Office of Workers' Compensation Programs, does not have a role in the administration or oversight of state workers' compensation programs.

For the purpose of this training we will cover worker's comp under the Louisiana state section.

For further information see: www.dol.gov/owcp/

Family and Medical Leave Act (FMLA)

The Family and Medical Leave Act (FMLA) entitles eligible employees of covered employers to take unpaid, job-protected leave for specified family and medical reasons.

Small brokerages will not fall under the FMLA requirements and this discussion will not apply.

We will outline employer and employee requirements of FMLA so that you can determine if these regulations will apply to your situation.

Covered Employers

The FMLA only applies to employers that meet certain criteria.

A covered employer is a:

- 1) Private-sector employer, with 50 or more employees in 20 or more workweeks in the current or preceding calendar year, including a joint employer or successor in interest to a covered employer.
- 2) Public agency, including a local, state, or Federal government agency, regardless of the number of employees it employs.
- 3) Public or private elementary or secondary school, regardless of the number of employees it employs.

The short story here is – unless your brokerage employees 50 or more employees, FMLA will NOT apply to you and you will set your own policies regarding family leave.

Eligible Employees

Only eligible employees are entitled to take FMLA leave.

An eligible employee is one who:

- 1) Works for a covered employer
- 2) Has worked for that employer for at least 12 months.
- 3) Has at least 1,250 hours of service for the employer during the 12 month period immediately preceding the leave.
- 4) Works at a location where the employer has at least 50 employees within 75 miles.

As an employer, interested in the well-being of your staff, you should discuss with new employees on whether they are, or are not, covered under FMLA.

Leave entitlement

Eligible employees may take up to 12 workweeks of leave in a 12-month period for one or more of the following reasons:

- 1) The birth of a son or daughter or placement of a son or daughter with the employee for adoption or foster care.
- 2) To care for a spouse, son, daughter, or parent who has a serious health condition.
- 3) For a serious health condition that makes the employee unable to perform the essential functions of his or her job.
- 4) For any qualifying exigency arising out of the fact that a spouse, son, daughter, or parent is a military member on covered active duty or call to covered active duty status.

For more information regarding FMLA: www.dol.gov/whd/fmla/

Equal Employment Opportunity (EEO)

Equal Employment Opportunity laws prohibit specific types of job discrimination in certain workplaces.

Generally a private employer may not discriminate on the basis of race, color, religion, sex (including pregnancy), national origin, age (40 or older), disability or genetic information.

For more information regarding EEO: www.eeoc.gov

Age Discrimination in Employment Act (ADEA)

Protects certain applicants and employees 40 years of age and older from discrimination on the basis of age in hiring, promotion, discharge, compensation, or terms, conditions or privileges of employment.

The ADEA is enforced by the Equal Employment Opportunity Commission (EEOC).

For more information regarding ADEA: www.eeoc.gov/laws/types/age.cfm

Americans with Disabilities Act (ADA)

The Americans with Disabilities Act of 1990 prohibits private employers, state and local governments, employment agencies and labor unions from discriminating against qualified individuals with disabilities in job application procedures, hiring, firing, advancement, compensation, job training, and other terms, conditions, and privileges of employment.

For more information regarding ADA: www.eeoc.gov/laws/types/disability.cfm

Summary – federal laws

Although Federal laws concerning employment matters are pretty straightforward, it's important you have a thorough understanding of the legal demands.

This is where your small business advisors can be invaluable. Communicating your policies along these lines will go a long way to protecting your business from exposure.

Later in this lesson we will cover communicating to your employers their responsibilities as they relate to federal and state laws. You will do this by providing a thorough policies and procedures to your employees and contractors.

Employment Law - State

Employment laws in the State of Louisiana are closely aligned with Federal statutes.

For detailed information about the regulations in the state, refer to: <http://www.lawworks.net/>

There are a few areas of employment law in Louisiana where you should have a basic familiarity. These are:

- Worker's compensation
- Unemployment insurance
- Anti-Discrimination statute
- Smoking discrimination statute

Workers compensation

Employees injured on the job are entitled to specific benefits under *workers compensation*.

The benefits may include medical care, wage benefits, rehabilitation services, or even death benefits.

As an employer you are obligated to provide these benefits and would be paid by you, directly to the employee, or more likely, your workers compensation insurer.

Every employee, full-time or part-time, shall be covered under workers comp from their first day of employment.

Employers, unless specifically approved as a self-insured entity, must be covered by workers compensation insurance.

The law covers a broad range of injuries, physical or mental, if the injury occurs within the scope of his or her employment.

For an expanded presentation of your responsibilities under the Workers Compensation laws, refer to the Louisiana Workforce Commission website at lawworks.net.

Unemployment insurance

Unemployment Insurance (UI) is a program that provides temporary financial assistance to workers who are unemployed through no fault of their own and who also meet the requirements of the Louisiana Employment Security Law.

UI benefits are paid as a matter of past employment and legal entitlement – not need.

In Louisiana, employers pay all of the costs of the UI program through a payroll tax or reimbursable program.

Employee wages are not used in any way to finance the UI program.

Further information regarding the UI regulations go to: www.lawworks.net

Anti-Discrimination and Anti-Retaliation Statute

Louisiana's anti-discrimination and anti-retaliation statute is very similar to the federal EEO requirements.

Like the federal statute, discrimination in employment based on race, color, religion, sex, national origin, disability, sickle cell trait, protected genetic information, and age (40 to 70 years old) is strictly forbidden.

Although Louisiana is a right-to-work state and you can end an employment relationship at any time without notice or reason, there are some statutory protections for employees given whistleblower status.

The scope of these protections go way beyond the purpose of this lesson. Should you believe this might be an issue when dealing with an employee you should definitely refer the question to your legal advisor prior to taking any employment action.

Smoking discrimination statute

In Louisiana, as long as an individual complies with applicable law and any adopted workplace policy regulating smoking, it shall be unlawful for an employer:

- 1) To discriminate against the individual with respect to discharge, compensation, promotion, any personnel action or other condition, or privilege of employment because the individual is a smoker or nonsmoker.
- 2) To require, as a condition of employment, that the individual abstain from smoking or otherwise using tobacco products outside the course of employment.

For the purpose of this statute a smoker is limited to a person who smokes tobacco.

Nothing in the statute precludes an employer from adopting a policy regulating the workplace use of tobacco product.

Violations of the statute shall mean a fine of \$250 and up to \$500 for each subsequent offense.

Workplace smoking laws apply to any enclosed workplace, excluding bars and outdoor patios. Louisiana does not require employers to create designated smoking areas or provide other accommodations for smokers or non-smokers in the workplace.

Licensed Agents

As a broker you are only as good as the agents you align with. Much of your time will be spent recruiting, developing, evaluating and replacing agents. You might be coach and mentor to one agent and five minutes later, drill sergeant to another.

A well thought out business plan spelling out the long-term goals and achievement milestones necessary to reach that goal, will dictate your staffing needs..

We will focus on two areas of staffing:

- Licensed agents
- Unlicensed assistants

Licensed real estate agent

Your agents will be the day-to-day sales face of your brokerage.

It's estimated that 80% of real estate sales agents will leave the business within their first two years. As a broker, you will have to strike a balance between hiring experienced, high-producing agents who can hit the ground running and taking risks on new agents with potential.

Here are some things to look for when recruiting agents:

- Experience –Seek out experienced agents looking for new opportunities. They are already trained and can bring their own relationships to your brokerage.
- Business acumen – Sales skills are important, but so is understanding the business fundamentals.

- Attract younger agents – The younger generation tends to be more tech savvy and can easily navigate the growing digital aspects of real estate.
- Continuing education – A solid training strategy can make your brokerage more attractive.

As managing broker you are responsible for the actions of your associate brokers and agents.

Your supervision activities should include:

- Making sure your agents are current with their license
- Be available to assist agents – Agents will inevitably encounter problems in their day-to-day activities – be there for them.
- Ensure advertisements meet legal requirements – That doesn't mean review every ad. It means make sure your agents understand the legal requirements.
- Keep agents advised of changes in real estate law.
- Provide a policies and procedures manual – When agents certify receipt of the manual they are acknowledging they understand what is expected of them. We will expand on the policies and procedure manual later in this lesson.

Employees - Unlicensed

Admin and agent assistants

Employees who assist brokers and agents are not licensed in Louisiana.

They are prohibited from:

- Hosting open houses
- Showing property
- Interpreting contracts or negotiating for buyers or sellers.
- Negotiating commissions and fees –

Generally any activity for which a real estate license is required is prohibited under penalty of law. They cannot be paid on any basis of real estate activity, such as a percentage of agent's commission.

Assistants can be invaluable in assisting agents by being a point of contact – answering the phone, managing correspondence, place listing signs on property, submit listings to MLS, act as a courier service to deliver documents or keys, and other administrative or clerical activities for which a license is not required. .

Names of unlicensed staff CANNOT be included on any brokerage team advertising.

Independent contractor

The most common model for broker/agent relationships is the Independent Contractor.

Benefits for the broker include:

- No income tax deductions
- No employment taxes
- No obligation to provide benefits
- No liability for workers comp
- Excluded from unemployment regulations

Benefits for the agent include:

- Can set own hours
- Has greater control of activities

- Greater opportunity for income
- Can choose where they work
- Controls their own destiny

A written independent contractor agreement should be executed prior to the agent performing any real estate sales activities for the broker.

The agreement spells out the items of agreement such as:

- Handling of listings
- Commission and compensation
- Agreement to abide by laws
- Expense and tax liabilities
- Supervision limitations
- Policies and Procedures – A place to acknowledge receipt of Policies and procedures manual should be on the agreement.
- Errors and Omissions Insurance – A place to acknowledge E&O coverage should be on the agreement.
- Termination

Make sure your agreement covers every area negotiated between you and your agent.

A sample contractor agreement can be found in the download resources for this lesson.

Commission and Compensation Management

The biggest factor in recruiting and retaining high producing agents is the compensation plan.

Most agents today are independent contractors with as little as 5% of agents today being full-time, on staff employees. The terms of independent contractor agreements have a wide range of negotiation to them, sometimes even within the same brokerage; higher producers demanding more favorable contracts.

What follows is a look at different compensation models in use today.

Agent Commissions – Split Commission 70/30

The most common model in use today is the *split commission* where the broker and agent split the commission made from the home sale.

Split percentages are typically defined in the independent contractor agreement. For this example we will use a common 70-30 split. Keep in mind this may vary between agents in the same brokerage based on what the broker and agent agreed to prior to executing the contractor agreement.

Let's say that Agent Andy sells a new home for \$300,000, and the commission rate on the sale is 6%,

The total commission on the sale would be \$18,000.

With a 70/30 split, Agent Andy gets 70% or \$12,600.

Broker Bob would receive 30% - \$5,400

Agent Commissions – 100% Commission

In the *100% commission* model, the agent pays the broker a monthly fee but retains 100% of sales commissions.

Again... Agent Andy sells a new home for \$300,000.

The commission rate on the sale is 6%,

The total commission on the sale would be \$18,000.

With a no commission split, Agent Andy keeps the full \$18,000. Andy is paying Broker Bob a monthly "Desk Fee" of \$1,200.

You may see variations of these, such as a plan where an agent starts out the year on a split commission model but if he or she hits a sales milestone, they change to a 100% plan. These are all subject to negotiation prior to the broker/agent agreement.

Generally, new agents are not interested in this model because of the monthly desk fee.

Agent Commissions – Referral Fees within same brokerage

In a sale where one agent referred the sale to another agent within the same brokerage a referral fee is usually paid.

Referring back to the \$300,000 sell at 6% - Agent Andy received the referral from Agent Amy. Per her contractor agreement she is to get 25% for referrals.

After the closing Broker Bob gets his 30% and the balance is split 75/25 between Andy and Amy.

Agent Commissions- Referral fees between brokers

Referral fees between brokerages come right “off-the-top” before the agent commission split.

In our \$300,000 example, Broker Bill in another state contacted Broker Bob and negotiated a 20% referral fee for his buyer for one of Bob’s listings

Agent Andy (still on the 70/30 plan) handled the sell.

After the closing, Broker Bob sends Broker Bill his 20% referral fee.

Leaving a balance of \$14,400 which is then subjected to the 70/30 commission split.

Agent Commissions – Franchise Fee

Major franchises usually charge a franchise fee right off-the-top of the full commission.

In our \$300,000 example, Broker Bob is affiliated with Big City Real Estate Franchise. The contract demands a 6% franchise fee off all closings. (Franchise fees are negotiated when executing the franchise contract)

At 6%, the franchise fee would be \$1,800.

Leaving a balance of \$16,200 which is then subjected to the 70/30 commission split, as shown.

There are some newer fixed-fee and fee-for-service listing brokerages that pay their agents a salary, rather than a commission.

Very few brokerages pay their agents a base salary but it’s not unheard of.

In summary, commission and compensation plans may vary widely between agents in your own brokerage. Consider what agents may bring to the brokerage when negotiating agreements.

Policy and Procedure Manual

Developing a thorough and concise Policy and Procedure manual for your brokerage is crucial to communicating performance requirements and standard procedures. In this section we’ll take a brief look at a sample manual you could adapt to your brokerage.

Why you need a Policy and Procedures manual

It’s very simple – to protect your brokerage. Having thorough written guidelines removes ambiguity from your business.

Face it, we’ve become a very litigious society and a clear policy/procedures manual will be your first line of defense.

The good news is you don’t have to start from scratch. There are many boiler-plate manuals available which can be a great starting point.

For our purpose we will use a Louisiana Real Estate Commission sample from 2000. This example is not provided as a doctoral document. You are encouraged to pick through it thoroughly, identify those topics important to you and adapt to your policy.

The topic of commission structures have been deliberately ignored in order to assure compliance with the federal Anti-Trust legislation. Therefore, fee policies, office hours and items of that nature should be added. Each broker determines the fee structure appropriate to the organization.

Considerations

Because policy and procedure topics can vary from brokerage to brokerage we will not cover specific bullets from the sample. We will speak in general terms the things you should consider when developing your policy and procedure guidelines.

- The manual should dictate a clear understanding of the broker/sales associates relationship, management and employees, and specific administrative and sales functions.
- Your insurance underwriter may require you to have a policy manual in place.
- The manual can minimize and resolve internal operational disputes.
- Consider how to deliver the manual to employees. You could have one copy available in the office. You could give a printed copy to each staff member. You could have an online copy for viewing. The key is how to best ensure that everyone has access to the manual and you have a mechanism in place to handle updates while at the same time managing costs.

LEGAL AND ADMINISTRATION RULES COMPLIANCE

OBJECTIVES

The legal and administration regulations for real estate brokers in Louisiana are extensive. This lesson covers all aspects of licensing and what penalties you might face should you violate LREC regulations.

We'll have a brief discussion on the recordkeeping requirements and end with a thorough overview of agency obligations

Upon completion of this lesson, you should understand:

1. All aspects of licensing.
2. Violations and disciplinary measures.
3. Recordkeeping and document control requirements.
4. The nature of agency relationships and duties.

Licensing

We'll open this lesson with a thorough examination of the real estate license processes:

1. Maintenance
2. Renewal
3. Reinstatement
4. Transfers
5. Changes to information
6. Exemptions
7. Activities requiring a license
8. License status

Licensing — Activities requiring a license

Since initial broker/salesperson licensing was covered in Lesson One we will focus on the activities that require a license as well as the process of maintaining and servicing licenses already held by agents.

Real estate activity means any action related to any portion of a real estate transaction, by one person for another, and for a fee or commission.

These activities may include:

- a) Sells, exchanges, purchases, manages, rents, or leases, or negotiates the sale, exchange, purchase, rental, or leasing of real estate.
- b) Offers or attempts or agrees to negotiate the sale, exchange, purchase, management, rental, or leasing of real estate.
- c) Lists or offers or attempts or agrees to list for sale or lease any real estate or the improvements thereon.
- d) Buys or offers to buy, sells or offers to sell, or otherwise deals in options on real estate or the improvements thereon.
- e) Advertises or holds himself, itself, or themselves out as engaged in the business of selling, exchanging, purchasing, managing, renting, or leasing real estate.
- f) Assists or directs in procuring prospects or the negotiation or closing of any transaction, other than mortgage financing, which results or is calculated to result in the sale, exchange, managing, leasing, or renting of any real estate.
- g) Is engaged in the business of charging an advance fee or contracting for collection of a fee in connection with any contract to promote the sale, exchange, purchase, rental, or leasing of real estate through a listing.
- h) Sells or attempts to sell or offers or attempts to negotiate the sale of any business whose assets include real estate or leases of real estate.
- i) Lists or offers or attempts or agrees to list for sale any business whose assets include real estate or leases of real estate.

Licensing — Maintenance

To maintain your license there are specific post-licensing and education requirements to.

- All initial licensees are required to complete forty-five (45) post-license education hours within one hundred eighty (180) days after the initial license date. Post-licensing education courses are available through LREC approved education providers.
- All active real estate licensees must complete twelve (12) hours of approved continuing education (CE) course work each year to be eligible to renew their license for the next year.
- Four (4) of the twelve (12) CE hours must be completed in mandatory subjects specified by the LREC.

Licensing — Renewal

Real estate salesperson and/or broker licenses are issued for a period of one year and expires on December 31st following the date of issue.

To renew the licensee may simply pay the prevailing renewal fee to the LREC.

Licenses, not renewed by January 1st are considered expired.

Should a licensee allow his license to expire, performance of any of the previously described real estate activities is unlawful. Should a sponsoring broker allow his or her license to expire, all associate brokers and agents under that license are prohibited from performing real estate sales activities as well.

Bottom line... don't let your license expire.

Licensing — Reinstatement

For a three month period following expiration the licensee may reinstate by paying the renewal fee, a delinquent fee and filing a renewal application.

The delinquent fee from January 1st through February 15th is one-fourth the fee between February 16th and March 31st. Delinquent renewals can get expensive.

Should a licensee fail to renew the license in this delinquent period the renewal right is forfeited.

He or she would then need to meet all the requirements of an initial applicant.

Licensing — Transfers

When an associate broker or salesperson ends association with a sponsoring broker, his/her license must be returned to the LREC within five (5) days of the termination date.

Once the license has been dispatched to the commission those licensees are prohibited, either directly or indirectly, from performing any real estate activity under authority of such license.

Upon sponsorship by another licensed broker, licensees are entitled to transfer the license to the new broker by written request and paying the prevailing transfer fee.

When the designated qualifying broker with a corporation, LLC, or partnership is terminated by either party for any reason, the following actions shall be taken:

- a) The qualifying broker must notify all associate brokers and salesperson sponsored by him in writing by certified or registered mail of the termination and the effective date of the termination.
- b) The organization or associate broker or salesperson sponsored by the terminated designated qualifying broker, shall engage in any real estate activity requiring licensing until a new qualifying broker has been placed and has been reflected in the commission's files.
- c) Upon designation of a new qualifying broker, the outgoing broker shall deliver the licenses of all sponsored licensees to the new qualifying broker.
- d) The new designated qualifying broker shall inform all associate brokers or salespersons in the organization, in writing by certified or registered mail, of his designation as qualifying broker no more than five days following the effective designation date.
- e) The outgoing qualifying broker shall return his license as qualifying broker to the commission within five days following the effective date of the designation of the new qualifying broker.

Licensing — Changes to Information

The commission shall be notified in writing within 10 days of any change in a licensee's mailing address, physical address or telephone number.

Licensing — Exemptions

The commission may exempt an applicant from certain licensing requirements if he/she has previous license history in another jurisdiction.

The applicant must request the exemption in writing and must include contact information, detailed license history, and all pre and post licensing education.

They must also indicate any previous or pending disciplinary action against them.

Partial credit may be granted for real estate courses completed in other licensing jurisdictions. No substitution will be allowed for the 30-hour portion of the 150-hour broker pre-licensing course.

Credit for real estate courses completed at a college or university will be granted by the LREC based on the applicability of the subject to the current pre-licensing course requirements.

The applicant must submit an original transcript to the LREC with a written request for a review toward the broker pre-licensing educational requirements.

Licensed real estate brokers or salespersons residing in a state whose appropriate authority has entered into a reciprocal agreement with the commission shall be granted an equivalent non-resident license by:

1. Providing LREC with sufficient proof of resident state licensing
2. Paying the Louisiana license fee
3. File an irrevocable agent appointment for process service with the LREC

They must also show a certificate of authority to do business in Louisiana and a certificate of registry as a foreign partnership from the Louisiana Secretary of State and providing the commission with copies of both.

Licensing — License Status

Licensees in good standing with the commission may elect to put their license in an inactive status.

This is done by:

- Apply for inactive status transfer
- Remitting the applicable fee

While the license is inactive, the licensee may not engage in any activity requiring a real estate license.

The licensee shall be required to renew the inactive license on a yearly basis by filing the required renewal application and paying the annual inactive renewal fees as specified in this Chapter.

The licensee may request transfer from inactive status to active status any time, provided the inactive license has been renewed and is current at the time the request is received at the commission.

An inactive licensee is not required to fulfill the continuing education requirement established for active licensees on a yearly basis.

Licensees remaining in the inactive status from one to five years shall complete the number of hours of CE specified below:

- 1-3 years inactive: 20 hours of CE
- 3-5 years inactive: 40 hours of CE

Additionally, if the license remains inactive for two to five renewal periods, he must also complete a four-hour course covering Louisiana real estate license law and commission rules and regulations as part of the hours previously specified to be eligible to return to active license status.

This required four-hour course must be completed within one year prior to the date of the transfer of the license to the active status.

The licensee may remain in the inactive license status indefinitely, provided he complies with the yearly inactive renewal procedures.

Licensees remaining inactive for more than five years are required to complete a maximum of eighty hours of approved CE within the five-year period immediately preceding the request to return to active license status.

Such continuing education shall include the four-hour Louisiana real estate license law and commission rules and regulations course which must be completed within one year prior to the date of the transfer of the license to the active status.

Any applicant who has continued to obtain continuing education in the required areas during the inactive period may cumulate those hours and be eligible to reactivate his license at any time.

Violations and Disciplinary Measures

In this next section we will take a look at the violations and disciplinary measures you and your agents may be subject to as a result of violations. Specifically we will go over:

1. Violations
2. Penalties
3. Administrative Actions
4. Investigations and hearings

Violations

The Louisiana Real Estate Commission Rules and Regulations are found in Title 46 LXVII: These are the Professional and Occupational Standards for Louisiana. The first chapter reads:

- The rules and regulations of the Louisiana Real Estate Commission contained herein have been adopted pursuant to and in compliance with R.S. 37:1430 et seq., and **ANY** violation of these rules or regulations, or of any real estate licensing law, shall be sufficient cause for any disciplinary action permitted by law.

In short any deviation from the Louisiana Real Estate rules and regulations and licensing statutes can be considered a violation and subject to disciplinary action.

Oliver Wendell Holmes famously said: *Ignorance of the law is no excuse.*"

For real estate professionals in Louisiana that concept is specifically addressed by Section 4301 of the Rules and Regulations - **Knowledge of the Law** – which states:

"It shall be the duty of all licensees, certificate holders, and registrants to have knowledge and be aware of all laws regulating the real estate industry in Louisiana including, but not limited to, these rules and regulations and the Louisiana Real Estate License Law as set forth in Chapter 17, Title 37 of the Louisiana Revised Statutes."

If you don't want to find yourself in violation of the law it's imperative that you study and know the law.

There are several additional violations listed in *Section 1455 – Causes for censure, suspension, or revocation of license, registration, or certification*. (Found in the resources documents download folder) We'll highlight several of these on those on the following slides.

For a complete list of those violations, please refer to this document for other violations that you could be subject to.

What follows is a sampling of those regulations.

- Failure to account for any money coming into his possession belonging to others. (§1455-4)
- Failure to properly disburse money which belongs to others upon its coming into his possession. (§1455-5)
- Commingling the money or other property of his principals with his own. (§1455-6)
- Guaranteeing or authorizing any person to guarantee future profits which may result from the resale of real property. (§1455-10)
- Knowingly making any false representations to any party in a real estate transaction. (§1455-15)
- Acting for more than one party in a real estate transaction without the written acknowledgment of all parties to the transaction. (§1455-16)
- Knowingly permitting a sponsored licensee or an employee to conduct real estate activities in violation of this Chapter. (§1455-20)
- Failure to reduce a bona fide offer to writing when a proposed purchaser requests that a written offer be submitted. (§1455-26)
- Failure to disclose to a buyer a known material defect regarding the condition of real estate of which a broker, salesperson, or timeshare interest salesperson has knowledge. (§1455-27)

- Having been finally adjudicated and found guilty for refusing, because of race, color, national origin, sex, or ethnic group, to show, sell, or rent any real estate for sale or rent to qualified purchasers or renters or for any violation of the Fair Housing Act of 1968 or the Louisiana Equal Housing Opportunity Act¹ and/or any amendments thereto or any successor legislation subsequently following. (§1455-28)
- Refusing to appear or testify under oath at any hearing held by the commission. (§1455-30)
- Failure to comply with an order or consent order issued or approved by the commission pursuant to adjudicatory proceedings. (§1455-32)
- Using advertising that is misleading or inaccurate. (§1455-34)

Investigations and Hearings

The LREC is bound by law to investigate any complaint submitted in writing.

Complaints may be filed against:

- Licensed Real Estate Brokers
- Licensed Real Estate Salespersons
- Registered Timeshare Developers
- Registered Timeshare Salespersons
- Certified Real Estate Schools
- Certified Real Estate Instructors
- Certified Louisiana Education Vendors

The Commission may not intervene, provide advice, or act on behalf of licensees or the general public in the following areas:

- Disputes between licensees over the payment or division of a commission
- Escrow deposit disputes
- Interpretation of contracts
- Issues related to the Law of Agency (breach of trust or fiduciary responsibility)
- Ethical or business practices of a licensee

Upon receipt of a valid case that falls within the jurisdiction of the LREC, a case file is opened and assigned to an investigator.

The investigator interview all individuals relevant to the case and examine all associated documents.

Licensees, registrants and certificate holders are required by law to cooperate fully with the investigation.

If an investigation reveals evidence of a violation of Louisiana Real Estate License Law or the Rules and Regulations of the LREC, a public adjudicatory hearing is scheduled.

All formal hearings are conducted in open meetings, in accordance with the Louisiana Administrative Procedure Act.

Persons involved in the investigation may be subpoenaed to attend the hearing. Licensees, registrants and certificate holders who are the subject of the hearing may be represented by legal counsel at their own expense.

The Commission renders a decision based upon all evidence presented at the hearings.

A finding of guilt can result in any of or combination of the following:

- Censure
- Revocation
- Suspension
- Levy of a fine
- Require additional education

It should be noted that the respondent may be assessed the administrative costs of the proceeding. Payment of these costs shall be a condition of satisfying any order issued by the commission. (per section 4113)

The commission will entertain a request for a reconsideration or rehearing if the request is postmarked or received at the commission within ten (10) days from the date of entry of the commission's order.

The request shall be reviewed by the commission attorney for compliance with the Administrative Procedure Act.

A finding by the commission attorney that the request does not establish grounds for rehearing, reopening or reconsideration shall result in a denial of the request.

Additionally, or in lieu of, the respondent may file a petition for judicial review in the Nineteenth Judicial District Court in the parish of East Baton Rouge. This must be done within 30 days to meet the filing deadline.

Penalties

A violation of the provisions of the licensing or real estate regulations could result in a fine of not more than two-thousand dollars or imprisoned not more than five years, or both.

A person who performs any real estate activity without a license may be liable for as much as a five- thousand dollar penalty.

Administrative Actions

The Investigation Division has the authority to issue simple citations which expedites the adjudicatory process and holds down costs for the licensee.

Citations can be issued for advertising violations as well as for other common violations. By not having to appear before a hearing the licensee saves a substantial penalty and can simply pay the fine and move on. Licensees wishing to avoid citations should be very familiar with all Commission's Rules and Regulations and licensing requirements.

Recordkeeping

In this section, there will be a brief overview of the documentation retention and escrow account requirements.

We will discuss document retention and client accounts.

Brokers shall maintain properly indexed documents pertaining to any real estate transaction for a period of five years.

These include:

- Copies of listing agreements
- Purchase agreements
- Property disclosures
- Lead-based paint disclosures
- Any contract amendments
- Banking transaction records
- Escrow account information

Client accounts

A resident broker, including corporations, partnerships and limited liability companies, who accepts any funds on behalf of clients in a real estate sales transaction shall open and maintain a **sales escrow** checking account in a financial institution in the state of Louisiana.

All sales escrow accounts shall be titled in the identical wording as stated on the broker's license and the wording "Sales Escrow Account" shall be imprinted on all checks and bank statements issued in connection with this account.

A resident broker, including corporations, partnerships and limited liability companies, engaged in the management of property owned by other persons shall open and maintain a **rental trust** checking account in a financial institution in the state of Louisiana.

All rental trust accounts shall be titled in the identical wording as stated on the broker's license and the wording "Rental Trust Account" shall be imprinted on all checks and bank statements issued in connection with this account.

A resident broker, including corporations, partnerships and limited liability companies, engaged in the collection of rental security or damage deposits in connection with property management activities on behalf of clients shall open a **security deposit trust** checking account in a financial institution in the state of Louisiana.

All security deposit trust accounts shall be titled in the identical wording as stated on the broker's license and the wording "Security Deposit Trust Account" shall be imprinted on all checks and bank statements issued in connection with this account.

Agency

In this section, we'll examine all aspects of Agency Relationships including Fiduciary Responsibilities, dual agencies, responsibilities to clients and much more.

Types of agencies

"Agency" means a relationship in which a real estate broker or licensee represents a client by the client's consent, whether express or implied, in an immovable property transaction.

There are four common types of agencies;

- Seller agency
- Buyer agency
- Dual agency
- Designated agency

A **seller agency** represents the seller in a real estate transaction.

In our example, the sellers have listed their home with Agent Amy as the selling agent. Amy must hold the best interest of the seller as her number one priority and is legally obligated to promote the home at the agreed to terms and timely present all offers to the seller, unless the seller has waived that duty. The agency must provide prompt and thorough accounting of all money or property transfers occurring out of this relationship.

A **buyer agency** represents the buyer in a real estate transaction.

Young newlyweds are ready to buy their first home. They have contracted with Agent Andy to help them find and purchase their new home. He is now legally obligated to work in the best interest of the buyer to find a property that meets their desires and to negotiate with sellers or their agents to get the buyers the best value and property.

Agent Andy may contact Agent Amy if the property that she represents meets his buyer's needs. They may go back and forth on negotiation, each trying to get the best deal for their client.

A **dual agency** represents both the buyer and the seller in a real estate transaction.

Looking back to our example where Agent Amy just signed a seller representation listing agreement. She may already be under contract with a buyer who this property would be a perfect fit. To represent both the buyer and seller as a dual agent Agent Amy must get informed written consent from both parties. We'll cover the specific and legal requirements of dual agency later in this lesson.

A **designated agency** simply means one broker represents both the buyer and the seller but has designated different agents to work with the buyer and the seller.

In our example Agent Amy and Agent Andy both work for Broker Bob who is the broker of record for this buyer and seller separately. He has designated Amy as the Seller Agent and Andy as the Buyer agent. The agency relationship shall be maintained by all licensees for their role in the real estate transaction.

Possible agency relationships in a single transaction

In any real estate transaction a licensee may be representing a buyer, a seller or both.

Fiduciary responsibilities

Fiduciary in basic terms means faithful servant.

An agent, whether buyer or seller, has a fiduciary relationship with their clients and are legally bound to work in their clients best interests.

A broker must ensure that agents engaged with clients and customers are meeting their fiduciary obligations.

Creation and disclosure of agency relationship

Creating an agency relationship begins, in the case of a seller, with a listing agreement; in the case of a buyer it would begin with an exclusive buyer agent contract.

Whenever a contract is entered into prospective sellers/lessors and buyers/lessees the agency disclosure informational pamphlet or the agency disclosure form must be provided.

Disclosure of acting as principle or other conflict of interest–

Licensees must disclose in writing to all principals in a real estate transaction the status of their license and any conflict of interest prior to entering into any real estate contract negotiations.

Responsibilities of agent to customers and third parties

Licensees have specific duties when representing clients, customers and other third parties.

1. A licensee must perform the terms of the brokerage agreement between a broker and the client.
2. A licensee must promote the best interests of the client by:
 - a. Seeking a transaction at the price and terms stated in the brokerage agreement or other terms that are acceptable to the client.
 - b. Timely presenting all offers to and from the client, unless the client has waived this duty.
 - c. Timely accounting for all money and property received in which the client has, may have, or should have had an interest.

A licensee representing a client does not breach a duty or obligation to the client by showing alternative properties to prospective buyers or tenants or by showing properties in which the client is interested to other prospective buyers or tenants.

A licensee representing a buyer or tenant client does not breach a duty or obligation to that client by working on the basis that the licensee shall receive a higher fee or compensation based on a higher selling price.

A licensee shall not be liable to a client for providing false information to the client if the false information was provided to the licensee by a customer unless the licensee knew or should have known the information was false.

Nothing in the regulations are construed as changing a licensee's legal duty as to negligent or fraudulent misrepresentation of material information.

The agency disclosure requirement does not apply to a lease that does not exceed a term of three years and under which no sale of the subject property to the lessee is contemplated.

Effect of dual agency on agent duties

A licensee may act as a dual agent only with the informed written consent of all clients. Informed consent shall be presumed to have been given by any client who signs a dual agency disclosure form prepared by the commission pursuant to its rules and regulations.

The form prepared by the commission shall include the following language:

"What a licensee shall do for clients when acting as a dual agent:

- (1) Treat all clients honestly.
- (2) Provide information about the property to the buyer or tenant.
- (3) Disclose all latent material defects in the property that are known to the licensee.
- (4) Disclose financial qualification of the buyer or tenant to the seller or landlord.
- (5) Explain real estate terms.
- (6) Help the buyer or tenant to arrange for property inspections.
- (7) Explain closing costs and procedures.
- (8) Help the buyer compare financing alternatives.
- (9) Provide information about comparable properties that have sold so both clients may make educated decisions on what price to accept or offer.

A licensee shall not disclose to clients when acting as a dual agent:

- a. Confidential information that the licensee may know about either of the clients, without that client's permission.
- b. The price the seller or landlord will take other than the listing price without the permission of the seller or landlord.
- c. The price the buyer or tenant is willing to pay without the permission of the buyer or tenant.

The dual agent agreement shall be obtained by a licensee from the client at the time the brokerage agreement is entered into or at any time before the licensee acts as a dual agent.

No cause of action shall arise on behalf of any person against a dual agent for making disclosures allowed or required by this Section, and the dual agent does not terminate any agency relationship by making the allowed or required disclosures.

In the case of dual agency, each client and licensee possess only actual knowledge and information.

There shall be no imputation of knowledge or information among or between the clients, brokers, or their affiliated licensees.

In any transaction, a licensee may without liability withdraw from representing a client who has not consented to a disclosed dual agency.

The withdrawal shall not prejudice the ability of the licensee to continue to represent the other client in the transaction or limit the licensee from representing the client in other transactions.

When a withdrawal occurs, the licensee shall not receive a referral fee for referring a client to another licensee unless written disclosure is made to both the withdrawing client and the client that continues to be represented by the licensee.

The dual-agency requirement does not apply if the licensee is the seller of property he owns, or if the property is owned by a real estate business of which the licensee is the sole proprietor and agent.

As before a dual agency shall not be construed to exist in a circumstance in which the licensee is working with both landlord and tenant as to a lease which does not exceed a term of three years and the licensee is the landlord.

Traditional Common Law Agency Duties (COALD)

The common law agency duties are the fiduciary responsibilities the salesperson or broker has in the relationship with their client.

These duties are commonly expressed as:

- **Care** – The agent must apply every skill to the best of their ability on behalf of the client.
- **Obedience** – The agent must obey all lawful orders given by the client.
- **Accounting** – The agent must fully account for all entrusted funds and not commingle (combine) client/customer funds in any fashion with his or her personal and/or business funds.
- **Loyalty** – The agent must give undivided loyalty to the client and puts the client's interests ahead of their own.
- **Disclosure** – The agent is obligated to disclose to the client any information she receives that may benefit the client's negotiating position.

Termination of agency

There are several reasons that may drive the termination of the agency relationship. Some of the simplest actions that terminate a relationship:

- **Expiration** – The performance date terms on the contract expire
- **Completing the agreement terms** – The agent or broker has completed the required performance requirements and their work is done.
- **Termination by mutual agreement** – Both parties agree to end the contract without default regardless of performance to date.

Then there are circumstances where an agency is terminated by **Operation of Law**.

This could be anything driven by court action but many common reasons are:

- Foreclosure
- Bankruptcy
- Law suit
- Death of a principal
- Insanity

There could be a circumstance where one of the principals or the broker of record dies or is otherwise medically or mentally incapacitated during the contract term.

This immediately terminates the agency relationship.

The commission may appoint another individual real estate broker to complete, carry out, and enforce any contracts to which the impaired broker was a party.

The appointment must occur within five (5) days of the event.

CONTRACTS

OBJECTIVES

Every real estate transaction you will ever be a part of will involve contracts – Listing Agreements, Purchase and Sale Agreements, and Buyer Broker agreements, to name a few.

In this lesson we'll start with some general contract knowledge and then look at the specifics of different types of contracts you will be exposed to in your real estate brokerage on an almost daily basis.

Upon completion of this lesson, you should understand:

1. Types of contracts and how they are executed.
2. Listing Agreements.
3. Purchase and Sale Agreements.
4. Other common agreements

General knowledge

To begin looking at contracts we'll dig into some of general requirements and features:

1. Requirements for Validity
2. Types of Invalid contracts
3. When contract is Considered Performed/Discharged
4. Assignment and Novation
5. Breach of Contract and Remedies
6. Acceleration and Other Contract Clauses

Requirements for validity

There are specific components of any contract that defines its validity – these are:

- Consideration – simply put – Why are you entering into this contract?
- Offer and acceptance – an offer of contract must be agreed upon
- Legal purpose – It must not violate the law
- Capable parties – It means the parties must have the mental and legal capacity to enter into a contract.
- Mutual assent – also referred to as a “Meeting of the minds.” The parties must come together and agree on the terms of the contract.

Consideration is the benefit each party to the contract expects to get from the agreement.

For example when I walk into a diner and give them money for a hamburger, I expect a hamburger in return. The diner agrees to give me a hamburger in exchange for my money. It's an implied contract for purchase.

A consideration is generally one of two things:

1. It's an agreement to do something not legally obligated to do. Something such as buying a piece of property from another party.
2. An agreement to **not** do something that you have the absolute right to do. For an example an employment contract that involves a “Non-compete” clause or an agreement not to sue another party for an injury.

In some states a “Non-compete” clause may invalidate the contract itself because the state has deemed these clauses violate the right of free employment for an individual – so it's an illegal term of the contract.

An **offer and acceptance** occurs when one party makes a clear and definite offer to enter into a contract and the other party agrees by accepting the terms offered.

For example, if I see a car I like on Craigslist and I agree to give the owner \$2,000 for the car and the owner agrees to give me the title to the car upon receipt of the \$2,000, that's the offer and acceptance.

The contract must have a **legal purpose** and not violate any law, state, federal, or international statutes where the contracted consideration would put you in violation of those laws.

We've all heard the term – put out a contract – on somebody or contract with one person to kill another. Because murder is illegal, a contract in that case would have no legal purpose.

Another example is - Making a contract for a financial loan where the interest rates exceeds those allowed by law would also not have legal purpose.

To be legally binding the contract must be executed by **capable parties**. The following parties are generally considered not capable of entering into contract agreements:

- Minors – Persons under the age of 18 lack the capacity to make a contract. A minor who signs a contract can either honor it or void it. There are some exceptions. A minor cannot void a contract for necessities such as food, clothing or lodging.
- The mentally incapacitated – a person lacking mental capacity can void, or have a contract voided by a guardian, (except contracts for necessities). Mental capacity is defined as the party can understand the meaning and terms of the contract.
- Alcohol and drugs – People who are intoxicated are usually not considered incapacitated and courts generally rule they cannot void their contractual obligations. In cases where one party intentionally set out to intoxicate the other solely for the purpose of executing a contract, courts would likely void that contract.

An essential factor in any contract is **mutual assent**.

Consent is not mutual unless all parties agree explicitly on all aspects of the contract.

Mutual assent is typically established during the offer and acceptance. To decide whether the parties have assented to an agreement courts would examine both their words and deeds.

There are many ways to reach an agreement as there is no standard verbal formula or prescribed conduct which directly determines assent. In cases where the offer and acceptance cannot be identified, courts will look at offer and acceptance behaviors to make their legal determinations.

According to Section 10 of the United States Code:

"All agreements are contracts if they are made by the free consent of the parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void"

So the things that make a contract valid are:

1. The agreement must not be declared void
2. The intention must be to create a legal relationship
3. It must be a lawful object
4. The offer, acceptance and consideration must be proper
5. The meaning must be clearly defined
6. Both parties must freely consent
7. All parties must have the legal capacity to form a contract
8. The consideration must be lawful
9. It must be done through legal formalities
10. The performance of contract must be possible

So then what are the things that would invalidate a contract?

In the eyes of the law two parties may have executed a contract in good faith (or not in good faith) and there are aspects of the circumstances that will invalidate the agreement.

- Lack of capacity
- Duress or undue influence
- Fraud or misrepresentation
- Nondisclosure
- Violation of public policy
- Impossibility
- Unconscionability

Minors and the mentally incapacitated legally **lack the capacity** to execute valid contracts. Courts, in most cases, will invalidate those contracts. For example:

A 17-year-old enters into a contract for a cell phone with a service fee of \$30 a month.

When the bill shows up the parent refuses to make the monthly payment. Because the contract was signed by a minor the contract is invalid and the debt uncollectable.

Although the minor is not obligated to pay for the phone, the parent or legal guardian should encourage the minor to return the phone to the provider..

Duress, or other coercion, will invalidate a contract when someone executed a contract agreement under threat of harm.

For example:

A delivery man is delivering a load of fish to a seafood restaurant. Economic duress occurs should the delivery man say something like:

"Pay me \$1,000 or I let the fish rot on the dock."

Undue influence would be something like saying: "You know me. We went to school together. You can trust me. Here... sign this contract."

If a **misrepresentation** occurred during contract negotiation it would likely be invalidated by legal action.

Misrepresentation would be telling a prospective home buyer the home is termite free when you know that to be untrue.

Nondisclosure is misrepresentation through silence or failing to disclose an important fact about the deal.

Nondisclosure would be NOT telling a prospective home buyer the home has a termite infestation when you know there is.

Contracts may be invalidated if they are found to **violate public policy**.

For example a landlord may not force a tenant to sign an agreement to not have a service animal such as a seeing eye dog on the property as this violates the Americans with Disabilities Act.

In some cases, a contract may be found unenforceable because it is **impossible** or impracticable to carry out.

There may be a valid purchase agreement contract on a home that was destroyed by a tornado before closing.

It would now be impossible to sell the home under the terms of the original contract.

Unconscionability means that something inherent in or about the agreement was so aggressively unfair most courts would invalidate the contract.

Within a contract is buried very complicated, technical language most people wouldn't understand or recognize. The party used a very small font and inserted the clause in such a way that would purposefully mislead the consumer into signing on unfair terms.

In this case, the contract might be declared unconscionable due to the unequal bargaining power between the parties, and the fact that one party used their knowledge and experience to take advantage of the other. If the court finds the contract unconscionable, it will be declared void and unenforceable.

A contract is considered **performed** when the contractual obligation is met.

For example you may contract with Dan the painter to paint your living room. When Dan finished the painting job he has met his contractual obligations. Unless the contract called for white paint and he painted it red.

Should one party fail to meet the requirement of the contract, (such as red walls instead of the contract agreed to white) then the contract is breached and the contractual obligations could be **discharged**.

In the case of the red walls with the contract breached you may not be required to pay Dan the painter - if that's the relief allowed in the contract.

You might be contractually obligated to allow Dan the option of making it right by painting it white. Everything is driven by the terms and conditions of the contract, even your rights should the contract be in breach.

A contract benefit might be transferred to a third-party by **assignment**. This doesn't transfer the contract obligations.

For example, Dan the Painter is obligated to paint the walls but may sub-contract to have Bob the painter to physically do the painting. He has effectively assigned the obligation of his contract with the homeowner to paint the walls to Bob but the burden of performance remains on Dan the painter.

In a **novation**, the third party picks up both the assignment and the burden of the contract obligations.

Effectively the original contract is extinguished and Bob the Painter gets a new contract obligating him to the performance obligations.

Breach of Contract

A cause of action where a contractual binding agreement is not honored by one or more parties to the contract.

Say for example you contracted with Paul the plumber to renovate the plumbing in your bathroom and he fails to complete the project he is in breach of the contract.

A contract breach is a civil wrong. A court may have to get involved to determine the remedy to the breach.

Breach of Contracts could be:

- Material
- Minor
- Fundamental

Breach of Contract - Material

A substantial breach of contract usually excusing the harmed party from further performance and giving him the right to sue for damages.

Type of breach is determined case-by-case with a court using six guidelines.

1. The extent to which the breaching party has already performed.
2. Whether the breach was intentional, negligent or the result of an innocent mistake.
3. How certain it is that the breaching party will perform the rest of the contract.
4. How much benefit of the contract the non-breaching party has gotten despite the breach.
5. The extent to which the innocent party can be compensated.
6. Difficulty on the breaching party if the court determined that the breach was material and the innocent party was under no obligation to perform his side of the bargain.

Say for example the plumber was contracted to replace the pipes in the homeowner's bathrooms.

The contract stipulated the use of copper pipes but instead he installed iron pipes. The court could determine that there was a material breach and rule that the homeowner can recover the cost of actually correcting the breach - taking out the iron pipes and replacing them with copper pipes.

Breach of Contract - Minor

Sometimes referred to as partial breach, it is less severe than a material breach and only gives the harmed party the right to sue for damages and usually does not excuse him from further performance.

In the case of our copper vs. iron pipe plumbing breach, a court, using the six guidelines, may determine that a minor rather than material breach occurred. In that case they may determine the homeowner can sue for the difference in the value of the home occurs based on having iron pipes versus copper pipes.

Fundamental Breach of Contract

A fundamental breach (or repudiatory breach) is a breach so fundamental that it permits the aggrieved party to terminate performance of the contract.

Suppose Plumber Bob used garden hose instead of copper pipe. That would be such a distinct violation with unacceptable materials any court would likely find a fundamental breach has occurred.

The breach is so “fundamental”, that the homeowner is deprived of the benefit of the contract and is entitled to stop performing and ...

The party is entitled to sue for damages.

Legal Remedy

Also known as judicial relief or judicial remedy.

This is where a court of law, exercising civil law jurisdiction, can enforce a right, impose a penalty, or makes a court order imposing the will of civil law.

This is where a court orders some kind of damages allowed in relief of a breach of contract or injury to another. The discussion of the different types of damages allowed by civil action are beyond the scope of this lesson. Just know that damages can be compensatory, incidental, punitive, liquidated or other legal remedies as determined by court order, normally by judicial decree but these could be set by a jury of peers.

Acceleration and Other Contract Clauses

An **acceleration clause** is a term that fully matures the contract performance due from a party upon a contract breach.

Clauses of conveyance, defects, prorations, possession, assignments and judgement are very common.

Listing Agreement

In this section we'll look at the different requirements for listing agreements and the major differences between exclusive and non-exclusive agreements.

A listing agreement is a written document signed by all owners of real estate or their authorized attorney in fact authorizing a broker to offer or advertise real estate described in such document for sale or lease on specified terms for a defined period of time and is only valid if signed by all owners or their authorized attorney.

A valid a listing agreement should include:

1. Start and end date of property listing.
2. The price the home should be listed.
3. How the broker is to be compensated.
4. Terms regarding how the fees are paid.

5. The broker's scope of authority regarding co-agreements with other brokers.
6. The broker's scope of authority regarding the existence of previous offers.

An exclusive listing gives an agent the exclusive right to sell the property and is entitled to the commission. If any buyer brings their own buyers agent the commission would be split however mutually arranged.

In an exclusive agreement the agent generally does all the marketing. Exclusive listing agreements are very common.

In a **non-exclusive agreement** the agent is entitled to the commission only if he sells the property.

Non-exclusive agreements come with inherent risk - many agents refuse to work with them. Consider a sales agent that advertises a non-exclusively listed property. If another agent sells that property the advertising and marketing fees are lost.

Purchase and Sale Agreements

Selling a home has become more complex than in years past. Agreements will contain seller disclosure statements, longer and more mysterious form agreements, and a whole host of environmental concerns have burdened the process with strict requirements.

In this section we'll discuss the general aspects of real estate purchase and sell agreements.

General requirements

First, a licensee must use the form prescribed by the Louisiana Real Estate Commission (LREC) and found on their web site.

Second, other than filling in blanks, no strike-outs or modifications of any kind can be made to the printed form.

Any modifications should be done by an attached addendum referencing the line number and changes made.

An offer becomes binding

A purchase and sell agreement is a nominate, bilateral, onerous contract, named in the Louisiana Civil Code as a Contract to Sell and in which both parties are obligated reciprocally and both parties receive an advantage in exchange for the obligation.

To be a binding contract no deposit or payment is required. It binds upon signature.

Offers and counter offers

When brokering real estate sales or purchases the broker/agent must ensure the following:

1. All written offers and counter offers for the purchase of real estate shall be presented to all buyers and/or sellers for their consideration and decision immediately, without delay.
2. The licensee who prepares an offer or counter offer in a real estate transaction shall ensure that the time of day and date the offer or counter offer was signed by the offering party are included in the document.
3. The licensee who presents an offer or counter offer in a real estate transaction shall ensure that the time of day and date the offer or counter offer was accepted, rejected or countered are included in the document.

Agents and brokers are legally bound to present offers and counter-offers in a timely manner.

Designated agents shall be responsible for making reasonable efforts to contact and notify the designated agent of the other party of the existence of an offer or counter offer.

The agent who transmits or delivers the written offer or counter offer must document the date, time of day, place, and method of delivery.

This documentation may include, but certainly not limited to, annotation by the delivering designated agent, a dated and timed facsimile transmission receipt or a dated and timed electronic mail receipt.

When a buyer or seller rejects an offer the agent must document date/time of the rejection and clearly mark on the document that it was rejected.

If the buyer/seller refuses to sign the offer rejection, the agent must certify that fact with the date and time stamp.

The rejected offer shall be returned to the prospective buyer and/or seller within five days after the offer document is signed.

If the seller has granted the authority to the listing agent to reject an offer or counter offer and the seller is not available the agent may mark the offer rejected, document the date and time and forward the document within five days.

Priority of Multiple Counteroffers

Remember that all written offers and counter offers must be presented for consideration and decision immediately, without delay.

When the agent receives counter offers on listing the only priority is to the best interest of the client and not the order the counter offer is received.

Consider this scenario...

Agent Amy receives a counter-offer on a home purchase at 4:00 pm.

She calls her seller immediately giving the terms of the offer.

The seller wants to think about it overnight and tells Amy they would talk about a decision in the morning and to call around 10am.

Later that evening, around 8pm, Agent Amy gets a slightly higher price offer from another buyer.

Amy calls the seller and gets voicemail. She leaves a message for the seller leaving the terms of the new offer on the voicemail and says she will call the next day at 10am to discuss. So now the seller has two offers to consider.

Amy calls the seller at 10am.

The seller has considered both offers and has decided to accept the offer that came in at 8pm.

Just because an offer comes in before another the time it is received should have no bearing on the seller's decision.

Contingencies

Another common component to a real estate offer is "Contingency." It ties the offer to something else happening for it to be acceptable.

Some of the more common are:

- Financing Contingency
- Appraisal Contingency
- Inspection Contingency
- Sale contingent on sale of current property.

Financing Contingency

This is one of the most common contingency you will see regularly.

Usually it is a very specific about terms of the financing.

For example the financing contingency might say something like this:

Buyer shall have 14 days from the date of the binding agreement to determine if buyer has the ability to obtain a loan with the following terms:

- Loan Amount: 90% of the total purchase price
- Term: 15 years
- Interest Rate: No Higher Than 5.0%
- Loan Type: FHA

If the Buyer is unable to obtain the loan with the specific terms described and notifies seller in writing of this within the Financing Contingency Period the agreement shall terminate without penalty to Buyer.

Appraisal Contingency

The appraisal contingency usually goes hand-in-hand with the financing contingency as the lender will not loan more than the appraised property value.

The appraisal contingency will normally read one of two ways...

1. If the property doesn't appraise at least as high as the purchase price, you can back out of the deal...or
2. If the property doesn't appraise at least as high as the purchase price, you can ask the Seller to drop the price, and if he refuses, you can then back out of the deal.

Inspection Contingency

Sometimes called a "Due Diligence Contingency." It's a period of time of anywhere from 3-14 days or more when a buyer can inspect the property to make sure he wants to buy it.

During this period the buyer can get a full property inspection and get bids from contractors to do any necessary repair work uncovered during this inspection. He can then either ask for a reduction in the sales price (or for the owner to do the repairs) or else just back out of the deal.

Contingency on Home Sale

This basically gives the Buyer the right to back out of the deal if he is unable sell his current residence.

Generally, the contingency is restricted to a specific time period when the contract is in effect, thereby giving the Buyer that amount of time to sell his other property.

This contingency is very common among homeowners going from one house to another. Not generally a contingency you would see on investment properties.

Some others that you might come across at some point include:

- Termite Contingency
- Lead Paint Test Contingency
- Deed Contingency
- Mold Inspection Contingency
- Sewer Inspection Contingency
- Insurance Contingency

Time is of the Essence

On the purchase and sales agreement at line 284 you will find the following verbiage:

DEADLINES: TIME IS OF THE ESSENCE and all deadlines are final, except where modifications, changes, or extensions are made in writing and signed by all parties to this Agreement. All "calendar days" as used in this Agreement shall end at 11:59 p.m. in Louisiana.

Essentially this statement drives a stake in the ground on times and dates of the contract and when the deadline is exceeded.

Other Common Agreements

In your brokerage career you will run across several different types of contracts including:

- Property Management Agreements
- Buyer Broker Agreements
- Lease and Lease Purchase Agreements
- Options and Right of First Refusal
- Rescission and Cancellation Agreements

We'll take a brief look at each of these understanding that you may encounter many other contracts outside this discussion throughout your career.

Property Management Agreements

A Property management contract is an agreement executed between a property owner and a property manager.

The owner employs the services of a property manager to operate, control, maintain, rent and lease a particular property.

Duties of the property manager may vary from contract to contract but the most common are:

1. **Collection and Disbursement**
Manager agrees to collect all rents as they become due and render the Owner a monthly accounting of rent income and expenses.
2. **Maintenance and Labor**
Manager agrees to maintain, repair and improve the property as needed and to hire and supervise employees and other contracted labor.
3. **Tenant screening and mgmt.**
The manager advertises for, screens and select tenants with suitable credit worthiness. The manager will set rents that reflect the market conditions and comparable rental properties.

Of course all duties and expectations will be clearly and concisely spelled out in the property management agreement. It is the sole determiner of what services you will or will not receive, what costs you will incur and your rights as outlined in the agreement.

When executing a property management contract you should ensure these items are covered.

- Responsibilities and Representations – This section will nail down the specific duties and expectations of both the owner and the manger. The contract should stipulate that the property manager is a direct representative of the owner.
- Contract Termination – Don't forget to leave ways out of the contract for reasons of non-performance, behaviors or as simple as wanting to make a change.
- Indemnification – This would define what the management company would and would not be liable for.

An agent hired by a buyer to help find a suitable property for purchase would typically execute a Buyer Broker agreement with that client.

Typically the buyer and the broker will enter into a contract defining their legal relationship. It explicitly covers the duties and responsibilities of both parties and sets out exactly what services the broker will be providing.

The three most common buyer broker contracts are:

- Nonexclusive not-for-compensation
- Nonexclusive right-to-represent
- Exclusive right-to-represent

Nonexclusive not-for-compensation agreement

In this common buyer-broker agreement the broker is not paid any commission.

Other common contract terms include verbiage that allows the buyer to retain multiple brokers and the contract to be revoked by either party at any time for any reason.

Nonexclusive right-to-represent agreement

Under this agreement compensation is only paid to the broker if the buyer decides to buy the house the broker proposes.

If a commission is paid to the broker by another party, this obligation is removed.

Usually these agreements may not be revoked except for specified reasons spelled out in the contract.

Exclusive right-to-represent agreement

Under this contract the buyer agrees to work exclusively with this broker and may not contract another.

It spells out the commission to be paid and is paid whether the broker, the owner or another broker finds the property ultimately purchased.

If the broker commission is paid by another party such as the seller, the buyer is not obligated to pay.

Lease and lease purchase agreements

Lease agreements sets out terms for landlords and tenants that will govern their rental relationship.

It usually includes things like:

- Tenant names
- Occupancy limits
- Length of tenancy
- Rent and deposit amounts
- Maintenance
- Restrictions

Lease and lease purchase agreements

A lease purchase agreement is simply a lease contract combined with an option giving the tenant the right purchase the property.

Some portion or all the rent payments made during the term of the lease could be applied to the down payment and used to purchase the home or real estate.

Options and Right of First Refusal

An **option** is a contracted right a property owner would give to another person to buy a property. The contract terms might include pricing and time period the option includes.

The **right of first refusal** obligates the property owner to offer the property to the holder upon the same terms as the owner proposes to sell to a third party.

The holder must wait for the seller to offer the property for sale. Once the property goes up for sale the holder of the refusal right must exercise his right within the time period specified in the contract. If the holder fails to do so the owner may then sell the property to another buyer.

Rescission and Cancellation Agreements

Rescission refers to a mutual agreement that terminates and discharges obligations owed under a contract.

All parties must mutually assent and restoration of the status quo is needed to effect rescission.

A **cancellation** nullifies a contract and extinguishes the liability of parties with respect to obligations which have yet to be performed.

Cancellation is distinguishable from rescission in that rescission restores the parties to the status quo, whereas cancellation terminates liability as of the time that a contract is canceled.

Keep in mind, if a contract is canceled, the parties remain liable for damages incurred prior to cancellation.

This is a sampling of some of the most common contracts you will encounter in your brokerage.

Other contracts you may see are:

- Employment contracts
- Service contracts
- Equipment leasing
- Insurance contracts
- Licensing agreements
- Nondisclosure agreements
- Power of Attorney

It's a good practice to draw on your attorney consultant to look over any contract you are considering prior to placing your signature at the bottom. Once signed, you are obligated. Your lawyer is the first line of defense against a bad contract.

PROPERTY MANAGEMENT

OBJECTIVES

You can choose many different specialties in the real estate business. The focus here will be on the function and requirements for property management.

Upon completion of this lesson, you should understand:

1. Agreements, duties and termination of property managers
2. The Louisiana Landlord and Tenant Act
3. Records and Receipts

Property Management

In this section we are going to talk about what it means to be a property manager and specific terms and sections of a property management agreement. We'll discuss the duties and legalities of the role.

Property Management Agreements

To start the discussion on property management it's important that we cover a couple of important distinctions.

Property Management means the marketing, leasing, or overall management of real property for others for a fee, commission, compensation, or other valuable consideration.

A property management firm usually manages multiple properties.

A **property manager** is someone who, for a fee, commission, or other valuable consideration, manages real estate, including the collection of rents, supervision of property maintenance, and accounting for fees received for another.

Property managers commonly focuses on one property but could also manage multiple properties.

These are the legal definitions straight out of the Louisiana licensing law, section 1431.

Any person managing, renting and/or leasing property in the State of Louisiana must have a valid broker's license.

These are all considered valid real estate activities under existing Louisiana real estate laws.

Any person paid to lease, rent, list, prospect tenants or negotiate, assist, or offer to perform any of those acts, needs to be licensed.

Persons that assist in property management tasks considered administrative, clerical or maintenance do not require a real estate license.

As a real estate broker you may be approached by a property management firm to act on their behalf as a property manager.

A property management agreement is not a formality – it's a legal necessity. It protects you, the property management firm and the property you will be managing.

It's a good time to engage your consulting attorney to sift through the terms of the agreement and advise you before signing it. This document will drive the services you will or will not receive, costs you will be responsible for and any and all rights you will have in the relationship, as well as the ways to can get out of the relationship.

There are dozens of boilerplate agreements out there with a wide range of terms and conditions.

We will focus on four key areas that should be found in any valid property management contract:

1. Responsibilities and Representations
2. Contract Termination
3. Indemnification
4. Boiler Plate legalese

The complexity of the agreement will dictate the length. Some agreements could be spelled out within a couple of pages. Others could be ten or more pages. The longer the agreement – the more imperative it becomes for your attorney to look it over and advise.

For the purpose of this lesson we will refer to the sample property management agreement downloaded for this lesson.

Responsibilities and Representations

It's common for the property manager to be the exclusive Agent of the owner of the property described on the agreement.

Section 1.1 of the sample reads:

1.1 Appointment and Acceptance

Owner hereby appoints Agent as sole and exclusive Agent of Owner to lease and manage the property described in paragraph 1.2 upon the terms and conditions provided herein. Agent accepts the appointment and agrees to furnish the services of its organization for the leasing and management of the Premises; and Owner agrees to pay all expenses in connection with those services.

The property affected by the agreement is described in the agreement in a very specific manner.

Section 1.2 of the sample reads:

1.2 Description of Premises

The Property to be managed by Agent under this Agreement is known as _____, located at _____, consisting of the land, buildings, and other improvements located at _____, in the State of _____.

The document will always dictate the term and renewal requirements of the agreement.

Section 1.3 of the sample reads:

1.3 Term

The term of this Agreement shall be for an initial period of _____ year(s) (the “initial term”) from the _____ to _____ and including the last day of _____, and thereafter shall be automatically renewed from year to year unless terminated as provided in sections 21 or 27 herein.

Each of said one-year renewal periods is referred to as a “term year.”

:

The agreement will also spell out how the Agent will be compensated for the property management.

Section 17.1 of the sample reads:

17.1 For Management Services

The greater of (i) \$ _____ per month or (ii) _____% of the total monthly gross receipts from the Premises, payable by the 25th day of the current month for the duration of this Agreement. Payments due Agent for periods of less than a calendar month shall be prorated over the number of days for which compensation is due. The percentage amount set forth in (ii) above shall be based upon the total gross receipts from the Premises during the preceding month.

Some Property Management Agreements may specify that the Agent is responsible for opening bank accounts for operating and reserve funds and another account for security deposits.

If the owner requires the agent to be bonded this will also be specified.

The agreement will usually be very specific about the agent's responsibilities for rent collection, security deposits and the property operating expenses.

Section 3.1 of the sample reads:

3.1 Agent's Authority

Agent shall collect (and give receipts for, if necessary) all rents, charges and other amounts receivable on Owner's account in connection with the management and operation of the Premises. Such receipts (except tenant's security deposits and advance rentals, which shall be handled as specified in paragraphs 2.2 and 3.3 hereof; and special charges, which shall be handled as specified in paragraphs 3.2 hereof) shall be deposited in the Operating (and/or) Reserve Account(s) maintained by Agent for the Premises.

Property owners typically define their needs for financial and operational reporting from the property manager.

Section 6 of the sample reads:

SECTION 6 FINANCIAL AND OTHER REPORTS

By the tenth day of each month, Agent shall furnish Owner with a statement of cash receipts and disbursements from the operation of the Premises during the previous month. In addition, Agent shall, on a mutually acceptable schedule, prepare and submit to Owner such other reports as are agreed on by both parties.

It is important for the Owner to review these statements each month. Monthly reports are held open to correct errors for 90 days, and then become final, subject to an annual audit that may be required by the Owner per paragraph 6.1.

It's also common to find verbiage that will allow the owner to audit the finances periodically to ensure complete disclosure of income and expenses.

Section 6.1 of the sample reads:

6.1 Owner's Right To Audit

Owner shall have the right to request periodic audits of all applicable accounts managed by Agent, and the cost of such audit(s) shall be paid by Owner.

Property managers are normally given responsibility over any advertising necessary for the rental and leasing of property.

Section 7 of the sample reads:

SECTION 7 ADVERTISING

Agent is authorized to advertise the Premises or portions thereof for rent, using periodicals, signs, plans, brochures, or displays, or such other means as Agent may deem proper and advisable. Agent is authorized to place signs on the Premises advertising the Premises for rent, provided such signs comply with applicable laws. The cost of such advertising shall be paid out of the Operating (and/or) Reserve Account(s). All advertising shall make clear that Agent is the manager and NOT the Owner of the Premises. Newspaper ads that share space with other properties managed by the Agent shall be prorated based on: **Actual lineage of the ad devoted to the Owner's property plus a prorated share of any headlines and/or signature lines.**

Duties of property rental and tenant management are inherent to any property management agreement.

Section 8.1 of the sample reads:

8.1 Agent's Authority to Lease Premises

Agent shall use all reasonable efforts to keep the Premises rented by procuring tenants for the Premises. Agent is authorized to negotiate, prepare, and execute all leases, including all renewals and extensions of leases (and expansions of space in the Premises, if applicable) and to cancel and modify existing leases. Agent shall execute all leases as agent for the Owner. All costs of leasing shall be paid out of the Operating (and/or) Reserve Account(s). No lease shall be in excess of _____ year(s) without written approval by Owner. The form of the lease shall be agreed upon by Owner and Agent.

The Agent is generally given the responsibility of hiring, supervising and terminating employees necessary to the daily operation and maintenance of the property.

Section 9.1 of the sample reads:

9.1 Agent's Authority to Hire

Agent is authorized to hire, supervise, discharge, and pay all servants, employees, contractors, or other personnel necessary to be employed in the management, maintenance, and operation of the Premises. All employees shall be deemed employees of the Owner, and Agent shall not be liable to Owner or others for any act or omission on the part of such employees.

Due to the legalities of labor management there is usually language in the agreement that defines Agent and Owner responsibilities and liabilities.

Section 9.5 of the sample reads:

9.5 Hold Harmless, Labor Laws

Agent shall be responsible for compliance with all applicable state or federal labor laws. Owner shall indemnify, defend, and save Agent harmless from all claims, investigations, and suits, or from Owner's actions or failures to act, with respect to any alleged or actual violation of state or federal labor laws. Owner's obligation with respect to such violation(s) shall include payment of all settlements, judgments, damages, liquidated damages, penalties, forfeitures, back pay awards, court costs, litigation expenses, and attorneys' fees.

The Agent's duties regarding property maintenance are typically spelled out in the agreement.

Section 10 of the sample reads:

SECTION 10 MAINTENANCE AND REPAIR

Agent is authorized to make or cause to be made, through contracted services or otherwise, all ordinary repairs and replacements reasonably necessary to preserve the Premises in its present condition and for the operating efficiency of the Premises, and all alterations required to comply with lease requirements, governmental regulations, or insurance requirements. Agent is also authorized to decorate the Premises and to purchase or rent, on Owner's behalf, all equipment, tools, appliances, materials, supplies, uniforms, and other items necessary for the management, maintenance, or operation of the Premises. Such maintenance and decorating expenses shall be paid out of the Operating (and/or) Reserve Account(s). This section applies except where decorating and/or maintenance are at tenants' expense as stipulated in a lease.

Other subsections regarding maintenance may be very specific about limits of expenditure, utilities, contracts and liability for personal injury claims.

The agreement usually sets the legal relationship between the Owner and the Agent. It's common to confirm that the Agent acts on behalf of the Owner and is not an employee.

Section 12 of the sample reads:

SECTION 12 RELATIONSHIP OF AGENT TO OWNER

The relationship of the parties to this Agreement shall be that of Principal and Agent, and all duties to be performed by Agent under this Agreement shall be for and on behalf of Owner, in Owner's name, and for Owner's account. In taking any action under this Agreement, Agent shall be acting only as Agent for Owner, and nothing in this Agreement shall be construed as creating a partnership, joint venture, or any other relationship between the parties to this Agreement except that of Principal and Agent, or as requiring Agent to bear any portion of losses arising out of or connected with the ownership or operation of the Premises. Nor shall Agent at any time during the period of this Agreement be considered a direct employee of Owner. Neither party shall have the power to bind or obligate the other except as expressly set forth in this Agreement, except that Agent is authorized to act with such additional authority and power as may be necessary to carry out the spirit and intent of this Agreement.

Another important section relates to the Owner representations and warranties to the current legal status of the property and the Owners role in the agreement.

Section 18 of the sample reads:

SECTION 18 REPRESENTATIONS

Owner represents and warrants: That Owner has full power and authority to enter this Agreement; that there are no written or oral agreements affecting the Premises other than tenant leases, copies of which have been furnished to Agent; that there are no recorded easements, restrictions, reservations, or rights of way which adversely affect the use of the Premises for the purposes intended under this Agreement; that to the best of Owner's knowledge, the property is zoned for the intended use; that all leasing and other permits for the operation of the Premises have been secured and are current; that the building and its construction and operation do not violate any applicable statutes, laws, ordinances, rules, regulations, orders, or the like (including, but not limited to, those pertaining to hazardous or toxic substances); that the building does not contain any asbestos, urea, formaldehyde, radon, or other toxic or hazardous substance; and that no unsafe condition exists.

Contract termination

It's critical that the property management agreement has very specific language regarding how and under what circumstances the agreement is terminated.

Some of these reasons to terminate include.

- Termination without cause
- Termination with cause
- Termination compensation
- Owner responsibilities
- Sale of Property

The ability for either party to terminate the contract at any time for any reason is normally written into these agreements which usually includes a time component.

Section 21.1 of the sample reads:

21.1 Termination by Either Party

This Agreement may be terminated by either Owner or Agent, with or without cause, at the end of the initial term or of any following term year upon the giving of 30 days' written notice prior to the end of said initial term or following term year.

Should either party breach the agreement, or fail to act as required, the agreement shall terminate.

Section 21.2 of the sample reads:

21.2 Termination for Cause

Notwithstanding the foregoing, this Agreement shall terminate in any event, and all obligations of the parties hereunder shall cease (except as to liabilities or obligations which have accrued or arisen prior to such termination, or which accrue pursuant to paragraph 21.3 as a result of such termination, and obligations to insure and indemnify), upon the occurrence of any of the following events:

The items that would breach the contract would always be spelled out in the agreement.

The termination clause usually defines compensation to be paid to the agent under the circumstances of the termination.

Section 21.3 of the sample reads:

21.3 Termination Compensation _____ Month Minimum

If (i) Owner terminates this Agreement before the end of the initial term of any subsequent term year as provided in paragraph 21.1 above for any reason other than for a breach by Agent under paragraph 21.2(a) above, or if (ii) Agent terminates this Agreement for a breach by Owner under paragraph 21.2(a) above or pursuant to the provisions of paragraphs 21.2(b) or 21.2(d) above, then in any such event, Owner shall be obligated to pay Agent as liquidated damages an amount equal to the management fee earned by Agent, as determined under paragraph 17.1 above, for the calendar month immediately preceding the month in which the notice is given to Agent or to Owner, multiplied by the number of months and/or port....

The termination generally dictates that the owner assumes any obligations in place at the time of termination and his responsibility to compensate agent for those obligations.

Section 21.4 of the sample reads:

21.4 Owner Responsible For Payments

Upon termination of or withdrawal from this Agreement, Owner shall assume the obligations of any contract or outstanding bill executed by Agent under this Agreement for and on behalf of Owner and responsibility for payment of all unpaid bills. In addition, Owner shall furnish Agent security, in an amount satisfactory to Agent, against any obligations or liabilities which Agent may have properly incurred on Owner's behalf under this Agreement.

Should the owner sale the property during the management agreement that contingency should also be planned for in the termination clauses.

Section 21.5 of the sample reads:

21.5 Sale of Premises

In the event that the Premises are sold by Owner during the period of this Agreement, Agent shall have exclusive rights of representation in the sale as stated in a specific sales agreement to be negotiated separately. Upon transfer of ownership, this Agreement shall terminate by mutual consent of Owner and Agent under the terms and conditions set forth below. **In the event of any sale, the Agent shall receive a _____% sales commission based on the gross sales price. This exclusive right-to-sell shall survive the termination of this agreement for 120 days.**

Indemnification

All property management agreements will include sections that addresses what the management company can and cannot be held liable for.

Indemnify: *To compensate for loss or damage; to provide security for financial reimbursement to an individual in case of a specified loss incurred by the person.*

It's important that indemnification clauses are included within the agreement. Liability could quickly overtake any benefit of the contract.

Section 13 of the sample reads:

SECTION 13 SAVE HARMLESS

Owner shall indemnify, defend, and save Agent harmless from all loss, damage, cost, expense (including attorneys' fees), liability, or claims for personal injury or property damage incurred or occurring in, on, or about the Premises.

Boiler plate legalese

In addition to specific information found in the agreement you will also find standard clauses related to legal protections for activities that could arise out of the performance of the contract.

We'll look at a sampling of those found within the sample agreement. You may see many more in use throughout property management agreements.

You may find a section that covers indemnification after termination.

Section 22 of the sample reads:

SECTION 22 INDEMNIFICATION SURVIVES TERMINATION

All representations and warranties of the parties contained herein shall survive the termination of this Agreement. All provisions of this Agreement that require Owner to have insured or to defend, reimburse, or indemnify Agent (including, but not limited to, paragraphs 2.1, 2.3, 5, 8.4, 9.2, 9.5, 13, 14, 15, 16, 17.7, 20, 21.3, and 21.4) shall survive any termination; and if Agent is or becomes involved in any proceeding or litigation by reason of having been Owner's Agent, such provisions shall apply as if this Agreement were still in effect.

A common boilerplate clause is – **Force Majeure**

Frees both parties from liability or obligation when an extraordinary event or circumstance beyond the control of the parties, such as a war, strike, riot, crime, or an event described by the legal term act of God.

SECTION 24 FORCE MAJEURE

Any delays in the performance of any obligation of Agent under this Agreement shall be excused to the extent that such delays are caused by wars, national emergencies, natural disasters, strikes, labor disputes, utility failures, governmental regulations, riots, adverse weather, and other similar causes not within the control of Agent, and any time periods required for performance shall be extended accordingly.

Another very common clause is the “COMPLETE AGREEMENT” clause. It effectively means: *anything the parties may actually have agreed upon, but is not written down in the contract, is null and void.*

SECTION 25 COMPLETE AGREEMENT

This Agreement, including any specified attachments, constitutes the entire agreement between Owner and Agent with respect to the management and operation of the Premises and supersedes and replaces any and all previous management agreements entered into or/and negotiated between Owner and Agent relating to the Premises covered by this Agreement. No change to this Agreement shall be valid unless made by supplemental written agreement executed and approved by Owner and Agent|

Most contracts include a “NOTICES” clause. This effectively states that any obligations and reports required by the contract must be in writing, who is to receive it and at what address it is to be sent.

SECTION 28 NOTICES

Any notices, demands, consents, and reports necessary or provided for under this Agreement shall be in writing and shall be addressed as follows, or at such other address as Owner and Agent individually may specify hereafter in writing:

This has been a small sampling of clauses you will likely see in contracts.

Other common boiler plate items you might see include:

- Assignment
- Attorney Fees
- Governing Law and Venue
- Waivers

Louisiana Landlord and Tennant Act

In this section we will cover the ins-and-outs of the Louisiana Landlord and Tennant Act, including...

- Deposits
- The Lease
- Landlord/Tenant Obligations
- Maintenance and Repairs
- Improvements
- Lessee Deposit Act
- Vacating the property
- Eviction
- Military Termination Rights

Deposits

To finalize the agreement to rent a property a prospective tenant commonly puts down a deposit.

This action obligates the tenant to take possession of the property on a specific date.

It also obligates the property manager to have the property available and ready for move in on that date.

Deposit

This is a pre-lease deposit that allows the landlord to take the property off the market while evaluating the prospective tenant's application.

The deposit is usually in addition to any application and/or administration fee charged by the property.

Some properties may set the deposit amount based on the prospective tenant's credit rating.

Should the tenant fail to take possession of the property as agreed he/she would typically forfeit the deposit.

Depending on the obligations defined in the lease agreement the tenant could be subject to other liabilities for the failure to occupy.

If the landlord does not have the property available at the agreed time the deposit must be returned to the tenant.

Again the lease agreement would define any further liability of the property management should this be the case.

Deposit amounts, application and administration fees, time frames taken to evaluate tenant's suitability and terms of the lease agreement may be widely different from property to property in Louisiana. .

Security/Damage Deposits

A security/damage deposit is commonly required by the landlord to satisfy nonpayment of rent or any other default, including physical damage to the property.

In many cases the pre-lease deposit becomes the security deposit.

Pet Deposit/Fee

It's common to find properties that allow pets, however the tenant is normally required to pay a pet deposit or fee.

The distinction between "Deposit" and "Fee" is important.

Money held as a pet deposit is recoverable by the tenant. Money held as a "pet fee or charge" is not covered by the Lessee's Deposit Act (covered later in this section) and may or may not be recoverable according to the terms of the lease.

Terms of pet policies used by properties are all over the map. Limits such as how many pets, pet weights and even breeds may be defined by the terms of the lease for any given property.

Inspection and Checklist

To protect both parties, landlord and tenant, it's common for the property to be inspected prior to putting down any deposit.

Any issues uncovered by the pre-lease inspection should be agreed to by landlord and tenant before the lease is executed.

The lease

A lease is an agreement which legally binds both the landlord and the tenant to the terms for a specified period of time.

A lease may be oral or written. Keep in mind oral agreements may be impossible to prove in court should a dispute arise but they are not illegal.

Terms and conditions of the lease are usually regulated by the agreement.

- **Fixed Term Lease:** The duration of the lease may be agreed upon by both the landlord and the tenant for a fixed period of time.
 - A fixed term lease usually runs for a year but can be for any time period stipulated in the agreement not to exceed ninety-nine (99) years.

- **Month-to-Month Lease:** If the duration of the lease is not stated in the agreement, then it is presumed by law to be month-to-month.
 - The tenant or the landlord may terminate or change the terms of the lease with ten (10) days written notice before the end of the month.

Renewal Clauses: Some leases contain automatic renewal clauses, which renew the lease for another term equal to the original term.

1. Either the tenant or the landlord can avoid automatic renewal by giving written notice of his/her intent to vacate.
2. Most leases require written notice for termination at least 30 days prior to the current lease's expiration.

Without a Renewal Clause: If the tenant remains in the apartment for one week after the lease expires and there is no renewal clause, then the lease will automatically renew on a month-to-month basis.

In this situation, any change to the terms of the lease must be made with ten (10) days written notice prior to the end of the monthly period.

Non-Payment of Rent: Lease agreements normally allow for the landlord to charge a fee for the late payment of rent only if they are agreed to in the lease agreement.

If no written lease exists, fees cannot be charged unless they are agreed upon orally.

The law sets no specific amount for late fees; however, unreasonably high fees can be contested.

Other common lease rules:

- Most properties have occupancy rules governing the do's and don'ts of tenancy. These rules are usually agreed to on execution of the lease. These are things such as parking, quiet hours, occupancy limits and others.
- The death of either the landlord or the tenant does not dissolve the lease agreement. The heirs are bound by the agreement.
- The destruction of the property, without fault of either the landlord or the tenant, terminates the lease obligation.

Obligations of the Landlord

- To deliver the property to the tenant as agreed to in the lease agreement
- To maintain the property
- To protect the tenants right of possession during the lease term.
- To refrain from making any alterations to the property.
- To pay taxes, assessments and other charges to the property.
- To protect the tenant from lease changes resulting out of property sale during the term of the lease.

The tenant may have an action against the landlord for loss sustained as a result of the sale.

Obligations of the Tenant

- To pay the rent in accordance with the lease terms.
- To maintain the property, except for normal "wear and tear."
- To refrain from altering the premises without first obtaining written consent.

- To allow the landlord to make all necessary repairs.
- To use the property for the purpose for which it was leased.
- To inform the landlord when the property has been damaged or needs repair.

The tenant is liable for damages to the property that exceed the normal “wear and tear” caused by the tenant or the tenant’s guests.

Maintenance & Repairs

If a repair cannot be postponed until the end of the lease term, the tenant must allow the landlord to make these repairs, even if they are an inconvenience. However, a reduction in rent may be possible.

Should the landlord refuse to maintain the property or make necessary repairs after being notified, the tenant has options:

- The tenant can file a complaint with the Attorney General’s Consumer Protection Section
- Tenant can complain to local building officials when there are structural or hazardous defects.
- If a serious problem is ignored the tenant can terminate the lease

The tenant must be able to provide substantial proof of the landlord’s failure to act, or face serious financial and legal consequences.

Louisiana law allows tenants to pay for “necessary” repairs and to deduct the repair cost from the rent due or demand immediate reimbursement from the landlord.

In order to deduct repair costs, tenants must be able to prove each of the following:

- a) The repairs were necessary.
- b) The landlord failed to act within a reasonable time after being notified.
- c) The price paid was reasonable.

Improvements

At the termination of the lease, absent a contrary agreement, improvements, attachments or additions made by the tenant to the property are dealt with as follows:

The tenant may remove his/her improvements if he/she restores the property to its former condition.

If the tenant fails to remove the improvements, then:

- a) The landlord may pay the tenant for the cost of the improvements or for the enhanced value of the leased thing—whichever is less.
- b) The landlord may demand the tenant remove the improvements within a reasonable time and restore the property to its original condition.
- c) The landlord may remove the improvements and restore the property to its former condition at the expense of the tenant.
- d) The landlord may acquire the improvements without any obligation to reimburse the tenant.

From the property management perspective the key here is to keep records of all communication between the landlord and the tenant and to ensure these improvements were approved in the first place.

Lessee’s Deposit Act

The Lessee’s Deposit Act requires the landlord to return deposits within one month after the end of the lease, provided the tenant fulfilled the lease obligations and left a forwarding address.

If any part of the deposit is retained, the landlord must send the tenant an itemized list of deductions and any remaining balance within one month.

If the landlord fails to return the deposit or to send the itemized list within one month, the tenant may sue in Small Claims Court to recover the deposit.

If the landlord fails to account for the deposit within thirty (30) days of a tenant's written request for a refund, then the law allows the tenant to recover actual damages or \$200.00—whichever is greater.

The judge may also award court costs and attorney fees to the person who wins the suit. The law does not permit the tenant to give up, or waive, this right in a lease.

Vacating the property

The tenant must give proper **written notice** of his/her intent to vacate the property in accordance with the provisions of the lease.

If there is a month-to-month lease, then the tenant must give written notice of intent to vacate at least ten (10) days prior to the last day of the month for which the rent was paid.

If the lease agreement does not require specific cleaning, then the tenant must return the property in the same condition in which it was rented, allowing for normal wear and tear.

If the tenant fails to do so, then all or part of the deposit may be withheld.

If the property is not cleaned, then the landlord may deduct all or part of the cleaning charges from the deposit.

Clauses in a lease, which automatically deduct for cleaning, regardless of the property's condition, may be invalid.

Eviction

There are very specific procedures that must be strictly followed when evicting a tenant.

When the tenant breaches the lease agreement (*i.e., failure to pay rent*), the landlord must first deliver a written **Notice of Eviction** to the tenant.

This notice gives the tenant five (5) days, not counting weekends or holidays, to vacate.

If the tenant is not at home the notice may be posted on the door of the leased property. This has the same effect as delivering the notice to the tenant.

If a tenant fails to vacate within five (5) days of notice, then the landlord will begin eviction proceedings by filing a petition with the justice of the peace or city court.

The eviction trial will be heard three (3) days after the tenant has been served.

The tenant will then have to appear in court and state why he/she should or should not be ordered to vacate the property.

If the court finds the landlord entitled to evict the tenant, or if the tenant fails to appear at the trial, then the court will rule in favor of the landlord.

The tenant will be ordered to vacate the property within twenty-four (24) hours.

If the tenant fails to vacate the premises within twenty-four (24) hours after a judgment of eviction, the court must issue a warrant commanding the jurisdictional law enforcement agency to seize the leased property and remove the non-complying tenant.

A tenant who has appeared at the trial and argued a defense can file a suspensive appeal.

Perhaps the tenant has an affirmative defense like something the landlord filed in the eviction violates the law or is so untrue as to mitigate the right to evict ("I did not have the rent money" won't work).

The tenant must apply for an appeal bond, amount to be determined by the court, within twenty-four (24) hours.

This protects the landlord from losses should the tenant be unsuccessful in his appeal.

A landlord may file a separate suit to collect past due rent and may seize personal items, such as furniture and appliances, found in the property.

If the landlord is unable to locate the tenant, the court has a procedure which will still allow the landlord to get a judgment against the former tenant.

The landlord may get a court order to seize personal property found in the property without posting a bond or other security.

Military termination rights

Military service personnel have special protections under the Landlord and Tenant Laws.

Any active or reserve member of the armed forces, including the National Guard and the US Coast Guard, may terminate his/her lease if:

- a) The member receives orders to depart thirty-five (35) miles or more from the location of the dwelling.
- b) The member receives orders to depart thirty-five (35) miles or more from the location of the dwelling for more than three (3) months.
- c) The member is discharged, released, or retires.
- d) The member is ordered to reside in government-supplied quarters.
- e) The member is notified of the availability of government-supplied quarters which were not available at the time the lease was executed.

The member should have notified the landlord **in writing** that he/ she had a pending request for the government-supplied quarters *before* signing the lease.

Records and Receipts

This will be a brief discussion of what records should be maintained and how receipts should be handled in property management transactions.

A filing system to maintain all legal and supporting documents developed through the course of property management is crucial.

Records should be retained for no less than five (5) years.

- Lease agreements
- Financial records
- Intention to vacate letters
- Eviction records
- Maintenance records
- Accounts payable/receivable

This is not a definitive list but a view of some of the more crucial records to maintain. Because of the nature of the property management business there is always the risk of tenant disputes which could land you in court. Having a full history of correspondence, financial transactions, maintenance records and others could spell the difference between winning and losing a lawsuit.

Itemized receipts should be given tenants for any real estate transaction – rent payments, security deposit, pet deposit or any other transfer of funds.

Copies of receipts should be held for a minimum of five (5) years.

MANDATED DISCLOSURES

Property Condition Disclosure Form

In this section we will go through the requirements for the mandated Property disclosure form. We will point out the exemptions and sift through the form for a look at how the form should be used.

Sellers of residential real property must complete a property disclosure document in a form prescribed by the Louisiana Real Estate Commission (LREC), found at the commission's website.

The form describes several exemptions to this requirement.

1. Transfers ordered by a court, such as estate administration, foreclosure sale, bankruptcy, eminent domain or other actions of a court.
2. Transfers to a mortgagee by a mortgagor or successor in interest who is in default.
3. Transfers by a mortgagee who has acquired the property at a sale conducted pursuant to a power of sale under a mortgage or a sale pursuant to decree of foreclosure.
4. Transfers by a fiduciary in the course of administration of a decedent's estate, guardianship, conservatorship, or trust.
5. Transfers of newly constructed residential real property, which has never been occupied.
6. Transfers from one or more co-owners solely to one or more of the remaining co-owners.
7. Transfers pursuant to testate or intestate succession.
8. Transfers of residential real property that will be converted by the purchaser into a use other than residential use.
9. Transfers of residential real property to a spouse or relative in the line of consanguinity (blood line).
10. Transfers between spouses resulting from a judgment of divorce or separate maintenance or a property settlement agreement incidental to such a judgment.
11. Transfers or exchanges to or from any governmental entity.
12. Transfers from an entity that has acquired title or assignment of a real estate contract to a piece of residential real property to assist the prior owner in relocating, as long as the entity makes available to the purchaser a copy of the property disclosure statement, any inspection reports if any furnished to the entity by the prior owner, or both.
13. Transfers to an inter vivos trust.
14. Without additional consideration and without changing ownership or interest, confirm, correct, modify, or supplement a deed or conveyance previously recorded.

Seller must certify and sign that he is or is not required to execute the property condition form.

By claiming exemption the seller is also acknowledging that he is unaware of any property defects.

to assist the prior owner in relocating, as long as the entity makes available to the purchaser a copy of the property disclosure statement, any inspection reports if any furnished to the entity by the prior owner, or both.

(13) Transfers to an inter vivos trust.

(14) Acts that, without additional consideration and without changing ownership or ownership interest, confirm, correct, modify, or supplement a deed or conveyance previously recorded.

() ALL SELLERS are required to make disclosure of known defects regarding a property being transferred.

() SELLER acknowledges that SELLER is exempt from filling out the Property Disclosure Document and warrants that SELLER has no knowledge of defects to the property.

Seller (sign) _____ (print) _____ Date _____ Time _____

Seller (sign) _____ (print) _____ Date _____ Time _____

RIGHTS OF PURCHASER AND CONSEQUENCES FOR FAILURE TO DISCLOSE: If the property disclosure document is delivered after the purchaser makes an offer, the purchaser can terminate the pending purchase contract or withdraw the offer from the property.

On the downloaded Property Disclosure form:

Below the signature line on page one you will see RIGHTS OF PURCHASER AND CONSEQUENCES FOR FAILURE TO DISCLOSE, which reads:

If the property disclosure document is delivered after the purchaser makes an offer, the purchaser can terminate any resulting real estate contract or withdraw the offer for up to 72 hours after receipt of the Property Disclosure Document. This termination or withdrawal will always be without penalty to the purchaser and any deposit or earnest money must be promptly returned to the purchaser (despite any agreement to the contrary).

This sets a time window of 72 hours to deliver the property disclosure document or the purchaser has the right to withdraw the offer without penalty.

Next is the section: DUTIES OF REAL ESTATE LICENSEES AND CONSEQUENCES FOR FAILURE TO FULFILL SUCH DUTIES

Louisiana law requires real estate licensees to inform their clients of those clients' duties and rights in connection with the Property Disclosure Document discussed above. Failure to inform could subject the licensee to censure or suspension or revocation of their license, as well as fines. The licensee is not liable for any error, inaccuracy, or omission in a Property Disclosure Document, unless the person has actual knowledge of the error, inaccuracy, or omission by the seller.

This spells out the agent's legal obligation to truthfully inform clients his duties and their rights with regard to the Property Disclosure document.

OTHER IMPORTANT PROVISIONS OF THE LAW

This section highlights four important provisions of the property disclosure law. These are:

- A Property Disclosure Document shall not be considered a warranty by the seller.
- A Property Disclosure Document is for disclosure purposes only; it is not intended to be part of any contract between the seller and the purchaser.
- The Property Disclosure Document may not be used as a substitute for any inspections or warranties that the purchasers or seller may obtain.
- Nothing in this law precludes the rights or duties of a purchaser to inspect the physical condition of the property.

KEY DEFINITIONS AND INITIALS

KEY DEFINITIONS:		
<ul style="list-style-type: none">• Residential real property is real property consisting of one or not more than four residential dwelling units, which are buildings or structures each of which are occupied or intended for occupancy as single-family residences.• Known defect is a condition found within the property that was actually known by the seller and that results in one or all of the following:<ul style="list-style-type: none">(a) It has a substantial adverse effect on the value of the property.(b) It significantly impairs the health or safety of future occupants of the premises.(c) If not repaired, removed, or replaced, significantly shortens the expected normal life of the premises.		
RPDI Rev. 02/01/15	Buyer's Initials: _____	Seller's Initials: _____
		1 of 1

To be valid the seller and buyer must initial at the bottom of each page of the property disclosure form.

PROPERTY CONDITION.

The remaining pages of the Property Disclosure Form relate to very specific aspects of the property condition. Each section will include boxes to check "Yes", "No" or "Not Known".

Section 1: Land –anything related to the ground/air within the property boundaries.

Section 2: Termites and other wood-destroying organisms – You must acknowledge any termite damage.

Section 3: Structure – considers the current condition of anything related to the structure – walls, ceilings, roof, exterior... etc.

Section 4: Plumbing, water, gas, and sewerage

Section 5: Electrical, Heating and Cooling, Appliances

Section 6: Miscellaneous – this is a catch all section for anything else not covered above – storm damage, prone to flooding, zoning restrictions, etc...

Acknowledgements - This is the signature block where you acknowledge receipt and understanding of the disclosure.

Home Buyer Warranties

In this section we'll look at Home Buyer Warranties – what they mean, what they cost and what coverages they provide. .

A **Home Buyer Warranty** is specific insurance protection designed to cover the home structure, appliances and other items during a specific term of ownership. .

These insurance plans vary widely in cost and coverage. In practice the buyer must perform due diligence in understanding the coverage. .

Usually these warranties are very affordable in the \$200 to \$500 range for a year of protection.

At the end of the term they expire but they can usually be renewed at the prevailing rate at the time of renewal. .

Either party can purchase the coverage. The seller may include it to protect him from future repair calls from the buyer.

It's even a common practice that, because the coverage is so affordable, the real estate will provide the first year's coverage as a closing gift to the buyer. .

The warranty typically covers things like: .

- Air conditioning.
- Dishwashers.
- Doorbells.
- Furnace / heating.
- Water heater.
- Ductwork.
- Garbage disposal.
- Inside plumbing stoppages.
- Ceiling fans.
- Electrical systems.
- Range and oven.

The warranty usually does not cover:

- Pools and Spas
- Outdoor sprinklers
- Refrigerators, washers and dryers
- Haul aways

What Can Cause Denial of Payment?

- Improper maintenance
- Code violations
- Unusual wear and tear
- Improper installation

Agency Disclosure

The LREC has stated that agents are required to provide to buyers and sellers they represent a full disclosure of services and rights due as a result of the relationship. In this section we will look at those requirements and forms.

Agency Disclosure - §3703.A

Licensees shall provide the agency disclosure informational pamphlet or the agency disclosure form to all parties to a real estate transaction involving the sale or lease of real property.

You should have copies of both the form and the pamphlet.

Agency Disclosure - §3703.B

Licensees shall ensure that the pamphlets and forms are the most current versions prescribed by the commission and that reproductions of the pamphlet and form contain the identical language prescribed by the commission.

These means you should stay informed as to when the LREC is modifying and updating these documents.

Agency Disclosure - §3703.C

Licensees shall provide the agency disclosure informational pamphlet or the agency disclosure form to prospective sellers/lessors and buyers/lessees at the time when substantive contact is made between the licensee and customer, i.e. any specific financial qualifications of the customer or the motives or objectives in which the customer may divulge any confidential, personal or financial information, which, if disclosed to the other party to the transaction, could harm the party's bargaining position... when performing any real estate related activity involving the sale or lease of real property, other than a ministerial act as defined in R.S. 9:3891(12).

Agency Disclosure - §3703.D

Licensees providing agency disclosure informational pamphlets or agency disclosure forms to prospective sellers/lessors and buyers/lessees at the time when substantive contact is made shall ensure that the recipient signs and dates the pamphlet or form.

The licensee providing the pamphlet or form shall sign as a witness to the signature of the recipient, and the licensee shall retain the signed pamphlet or a copy of the form for a period of five years.

Agency Disclosure - §3703.E

Licensees providing agency disclosure informational pamphlets or agency disclosure forms to prospective sellers/lessors and buyers/lessees by email or other form of electronic transmission shall ensure that the recipient acknowledges receipt of the pamphlet or form by a document verifying the time and date of receipt.

As before, the licensee providing the pamphlet or form shall retain the signed pamphlet or a copy of the form for a period of five years.

Agency Disclosure - §3703.F

In any circumstance where one party (the seller/lessor or a buyer/lessee) refuses to sign the agency disclosure receipt for the pamphlet or form, or refuses to provide a document verifying receipt of the disclosure, the licensee shall prepare written documentation that includes the nature of the proposed real estate transaction, the time and date the pamphlet or form was provided and the reasons given for not signing the pamphlet or form, or providing a document verifying receipt of the pamphlet or form.

The document shall be retained for five years.

Agency Disclosure Form

Customer Information Form

What Customers Need to Know When Working With Real Estate Brokers or Licensees

This document describes the various types of agency relationships that can exist in real estate transactions.

AGENCY means a relationship in which a real estate broker or licensee represents a client by the client's consent, whether expressed or implied, in an immovable property transaction. An agency relationship is formed when a real estate licensee works for you in your best interest and represents you. Agency relationships can be formed with buyers/sellers and lessors/lessees.

DESIGNATED AGENCY means the agency relationship that shall be presumed to exist when a licensee engaged in any real estate transaction, except as otherwise provided in LA R.S. 9:3891, is working with a client, unless there is a written agreement providing for a different relationship.

- The law presumes that the real estate licensee you work with is your designated agent, unless you have a written agreement otherwise.
- No other licensees in the office work for you, unless disclosed and approved by you.
- You should confine your discussions of buying/selling to your designated agent or agents only.

DUAL AGENCY means an agency relationship in which a licensee is working with both buyer and seller or both landlord and tenant in the same transaction. Such a relationship shall not constitute dual agency if the licensee is the seller of property that he/she owns or if the property is owned by a real estate business of which the licensee is the sole proprietor and agent. A dual agency relationship shall not be construed to exist in a circumstance in which the licensee is working with both landlord and tenant as to a lease that does not exceed a term of three years and the licensee is the landlord. Dual agency is allowed only when informed consent is presumed to have been given by any client who signed the dual agency disclosure form prescribed by the Louisiana Real Estate Commission. Specific duties owed to both buyer/seller and lessor/lessee are:

- To treat all clients honestly.
- To provide factual information about the property.
- To disclose all latent material defects in the property that are known to them.
- To help the buyer compare financing options.
- To provide information about comparable properties that have sold, so that both clients may make educated buying/selling decisions.
- To disclose financial qualifications to the buyer/lessee to the seller/lessor.
- To explain real estate terms.
- To help buyers/lessees arrange for property inspections
- To explain closing costs and procedures.

CONFIDENTIAL INFORMATION means information obtained by a licensee from a client during the term of a brokerage agreement that was made confidential by the written request or written instruction of the client or is information the disclosure of which could materially harm the position of the client, unless at any time any of the following occur:

- The client permits the disclosure by word or conduct.
- The disclosure is required by law or would reveal serious defect.
- The information became public from a source other than the licensee.

By signing below you acknowledge that you have read and understand this form and that you are authorized to sign this form in the capacity in which you have signed.

Buyer/Lessee:	Seller/Lessor:
_____	_____
By: _____	By: _____
Title: _____	Title: _____
Date: _____	Date: _____
Licensee: _____	Licensee: _____
Date: _____	Date: _____

Agency Disclosure Pamphlet

- To help the buyer compare financing options.
 - To provide information about comparable properties that have sold, so both clients may make educated buying/selling decisions.
 - To disclose financial qualifications of the buyer/lessee to the seller/lessor.
 - To explain real estate terms.
 - To help buyers/lessees arrange for property inspections.
 - To explain closing costs and procedures.
- A dual agent **may not** disclose:
- Confidential information of one client to the other, without the client's permission.
 - The price the seller/lessor will take other than the listing price, without the permission of the seller/lessor.
 - The price the buyer/lessee is willing to pay, without the permission of the buyer/lessee.

CONFIDENTIAL INFORMATION

Confidential information means information obtained by a licensee from a client during the term of a brokerage agreement that was made confidential by the written request or written instruction of the client or is information the disclosure of which could materially harm the position of the client, unless at any time any of the following occurs:

- The client permits the disclosure by word or conduct.
- The disclosure is required by law or would reveal serious defect.
- The information becomes public from a source other than the licensee.

Confidential information **shall not** be considered to be about the physical condition of the property.

Confidential information can be disclosed by a designated agent to his broker for the purpose of seeking advice or assistance for the benefit of the client.

CONCLUSION

The Louisiana Real Estate License Law and the Louisiana Real Estate Commission Rules and Regulations require a real estate licensee to provide you with this informational pamphlet on brokerage agency relationships. For additional information on agency disclosure matters, visit the Louisiana Real Estate Commission website at:

www.lrec.state.la.us



Louisiana Real Estate Commission
Post Office Box 14785
Baton Rouge, LA 70898-4785
1-800-821-4529 (LA only)
1-225-925-1923

CUSTOMER INFORMATION PAMPHLET

*What Customers Need to Know
When Working With
Real Estate Brokers or Licensees*

As real estate transactions have become more complex and varied, real estate brokerage arrangements have evolved to meet the changing needs of customers entering this market. This pamphlet provides a description of the different types of brokerage arrangements available to customers, so that they may choose the brokerage services best suited to their needs.

Under Louisiana's real estate agency law, a licensee engaged in any real estate transaction shall be considered to be representing the person with whom he/she is working, unless there is a written agreement between the broker and the person providing that there is a different relationship or the licensee is performing only ministerial acts on behalf of the person.

A real estate broker and his/her associated licensees can provide valuable real estate services, whether in the form of basic customer services, or through client-level agency representation. The services you expect will depend upon the legal relationship you establish with the company. It is important for you to discuss the information contained inside with the real estate licensee, and to agree on whether your business relationship will be that of a customer or a client, and if a client, the type of agency relationship that will be in your best interest.

This information is provided in accordance with R.S. 37:1455 (A)(21) and R.S. 37:1467 to help you be more informed in the buying, selling, or leasing of real estate. In whatever manner you choose to be represented, the goal is generally the same. The real estate licensee is trying to assist you in the sale, purchase, or lease of real estate upon terms acceptable to all parties. For additional information, you may contact the Louisiana Real Estate Commission at 1-800-821-4529 or 1-225-925-1923.

REAL ESTATE FINANCING

OBJECTIVES

Without a way to finance property purchases most people would never be able to buy a home. Fortunately, mortgage banks and other financing outlets provide many different types of loan services for buying real estate. In this lesson we will look at the concepts of real estate financing, types and sources of loans, and laws regulating the mortgage loan business.

Upon completion of this lesson, you should understand:

1. Fundamental principles of real estate financing
2. Different types of loans available
3. Where to find property loans
4. Laws governing the credit and financing business

General Concepts of Real Estate Financing

On any day in the mortgage business prospective homeowners must navigate many different financing options and regulations. As a broker it is your bound duty to walk them through the process and get them the best financing arrangement you can. In the first section of this lesson we'll walk through the foundational concepts of real estate financing.

We'll discuss LTV ratios, Points and fees, Discounts and commissions, Mortgage insurance and a lot more.

LTV Ratio

A loan-to-value ratio is simply the ratio of money borrowed on a property to the property's fair market value.

For example:

$$\frac{\text{Mortgage Balance}}{\text{Home Value}} = \text{LTV Ratio}$$

The balance of the mortgage divided by the appraised value of the property will give you the LTV ratio.

So if you have a \$200,000 home with a loan balance of \$175,000

The LTV would be **87.5%**.

$$\frac{\$175,000}{\$200,000} = 87.5\%$$

Lenders use the LTV ratio as a way to judge the risk of making a particular mortgage loan.

A lower loan-to-value ratio is considered a lower risk to the lender.

Most conventional lenders put a cap on what the maximum LTV percentage they will loan.

There are subsidized loan programs which are geared specifically to high LTV loans or even 100% loans, such as VA.

Here are some example LTV calculations:

In this example the home appraised for more than the asking price, improving the LTV for the lender.

\$100,000 borrowed divided by the value of the home, \$130,000 = 76.9% LTV.

Home price:	\$120,000
Appraised value:	\$130,000
Down payment:	\$ 20,000
Loan amount:	\$100,000
Loan-to-value (LTV):	76.9 %

However, here the asking price is more than the appraised value. With the same loan amount, notice how the LTV is impacted.

\$100,000 divided by the value of the home, \$110,000 = 90.9% LTV.

Home price:	\$120,000
Appraised value:	\$110,000
Down payment:	\$ 20,000
Loan amount:	\$100,000
Loan-to-value (LTV):	90.9%

But what if you could only put \$10,000 instead of \$20,000 down. With an LTV of 100%, finding a lender may prove difficult without going to some form of government backed loan.

Home price:	\$120,000
Appraised value:	\$110,000
Down payment:	\$ 10,000
Loan amount:	\$110,000
Loan-to-value (LTV):	100.0 %

Points

A point is a fee equal to one-percent of the loan amount.

Loan amount:	\$ 200,000
Points @ 1% of loan	\$ 2,000

Points are generally charged for one of two reasons:

1. Origination points
2. Discount points

Origination Points

Some lenders may ask for points as compensation for their role in the loan transaction. Credit history is a factor in the amount of origination points a lender may charge.

Loan amount:	\$ 200,000
Origination points: 1.5	\$ 3,000

For this borrower, the lender has asked for 1.5 points on closing.

Since the amount of origination points asked for by the lender is not cast in stone, borrowers might be able to negotiate the amount of the origination points. In this case the lender would not negotiate and

The borrower would have to pay \$ 3,000 on closing.

Origination points are not tax deductible.

Discount Points

A lender might offer to lower the rate based on paying discount points up front. Lenders often give borrowers loan quotes that include loan rates and points.

For example:

Suppose you wanted to borrow \$200,000 for a 30 year loan. The lender offers a loan with a 4.0% rate which would make your monthly payment \$ 1,163.16.

The lender offered to discount the rate to 3.5% if two points were paid at closing.

2% of 200,000 = \$ 4,000.

This would lower the monthly payment and potentially save a lot of money. So let's consider how that looks over the life of the loan.

After paying the \$4,000 at closing the rate is adjusted to 3.8% and the loan now looks like:

The monthly payment is \$57.00 less after paying points.

It would take 71 months (5yrs – 11 months) for the borrower to recoup the \$4,000 in points paid at closing.

Discount points are a good deal for the borrower only if they remain in the home long enough to recoup the discount points paid at closing. In this example if they stayed in the home and paid the mortgage through the 30 year term, the total savings would be well over \$16,000.

Lenders benefit by receiving funds upfront rather than waiting for interest payments over time.

Broker Commissions

Brokers are paid a commission based on a percentage of the agent's commission for the sale.

It's important to understand that agents are licensed salespersons who work for and under the umbrella of a designated broker. They cannot work independently, and they are prohibited from being paid a commission directly by consumers.

Brokers, on the other hand, are able to work independently and/or hire real estate agents (salespersons). All commissions must be paid directly to a broker. The broker would then make the commission splits with any other agents involved in the transaction.

Let's review some of the commission plans presented in lesson three.

The most common model used today is the split commission where broker and agent split the sales commission. (70/30)

Split percentages are typically defined in the independent contractor agreement. For this example we will use a common 70-30 split. Keep in mind this may vary between agents in the same brokerage based on what the broker and agent agreed to prior to executing the contractor agreement.

Let's say that Agent Andy sells a new home for \$300,000, and the commission rate on the sale is 6%,

The total commission on the sale would be \$18,000.

With a 70/30 split, Agent Andy gets 70% or \$12,600.

Broker Bob would receive 30% - \$5,400

Another typical arrangement is the 100% commission model where the agent pays the broker a monthly fee but retains 100% of sales commissions.

Again... Agent Andy sells a new home for \$300,000.

The commission rate on the sale is 6%,

The total commission on the sale would be \$18,000.

With a no commission split, Agent Andy keeps the full \$18,000.

Andy is paying Broker Bob a monthly "Desk Fee" of \$1,200.

You may see variations of these, such as a plan where an agent starts out the year on a split commission model but if he or she hits a sales milestone, they change to a 100% plan. These are all subject to negotiation prior to the broker/agent agreement.

Generally, new agents are not interested in this model because of the monthly desk fee.

The broker's compensation is specified in the listing agreement. The rate of the broker's commission is usually negotiable.

In fact, it is a violation of federal antitrust laws for agents and brokers to attempt in any fashion to impose uniform commission rates.

Commissions are taken out of the sale proceeds, and it's usually the seller who pays the commission, unless the buyer and seller negotiate a split.

Most sellers factor the commission into the asking price. The buyer is paying at least some of the commission because of the higher asking price.

Mortgage Insurance Premiums (MIP)

Mortgage insurance premium (MIP), is an insurance policy used in FHA loans if the down payment is less than 20%.

The FHA assesses either an "upfront" MIP (UFMIP) at the time of closing, or an annual MIP, calculated every year and paid in monthly installments.

The rate for an annual MIP depends on the term of the loan and the LTV. Should the loan balance exceed \$625,500, a higher percentage will be owed.

Lender Requirements

Most lenders have very specific qualifying parameters for approving mortgage loans.

Although the basic factors are common to all lenders, there may be some minor variances in the levels of each parameter. For example one lender may require a 720 FICO score and another may require 740.

The most common factors include:

- Credit score
- Household income and expenses One significant determining factor is the debt-to-income ratio
- Employment history – Looking for job stability
- Assets – What's the net worth of the buyer?
- Collateral – Is the property valued above or below the loan price?
- Down payment – This can vary widely from one loan product to the next.

Equity

Home equity is simply the value of the home with regards to ownership.

Equity increases as you pay down the mortgage. It also increases as the market value of the home increases.

To calculate equity, subtract the remaining mortgage balance from the appraised home value.

For example if you owed \$ 40,000 on a \$150,000 home your equity would be \$110,000.

Qualifying buyers

Qualifying the buyer is the first order of the business for the mortgage origination professional.

When approached by a borrower, some factors will be known and others must be determined based on:

- Income
- Debt
- Down Payment
- Maximum Qualifications

INCOME

Gross Monthly Income (GMI)

1. Salary – (wages from paychecks); year-to-date income divided by the effective months on the pay stub.
2. Self-Employed and Commission or Bonus Income – average the net income after expenses and gross adjusted income before taxes from Schedule “C” for the most current 2 years.

DEBTS

List of Monthly Obligations

1. For all debts (beginning with those on the credit report) use the minimum payments.
2. Add in debts not listed on the credit report and use minimum payment on the monthly statements or use 4% of the balance as the minimum required payment.

DOWN PAYMENT

1. US Dept. of Agriculture and VA allow \$0 down
2. FHA allows 3.5% down
3. Conventional uses 3% to 20 % down with private mortgage insurance (PMI)
4. With 20% down, PMI is not required

Maximum Qualifying for Conventional Loans

1. $GMI \times 35\% - \text{debts} = \text{Max PITI}$
2. We already know: $\text{Loan amount} \times \text{factor} = \text{P\&I}$
3. So: $\text{P\&I} / \text{Factor}$ is the Loan Amount
4. Therefore: $\text{PITI} - \text{Insurance \& Taxes} = \text{P\&I}$
 $\text{PITI} \times 70\%^* = \text{Estimated P\&I}$

* Insurance and taxes typically make up around 30% of a monthly mortgage payment.

Maximum Qualifying for FHA

1. $GMI \times 43\% - \text{debts} = \text{Max PITI}$
2. We already know: $\text{Loan amount} \times \text{factor} = \text{P\&I}$
3. So: $\text{P\&I} / \text{Factor}$ is the Loan Amount
4. Therefore: $\text{PITI} - \text{Insurance \& Taxes} = \text{P\&I}$
 $\text{PITI} \times 70\% = \text{Estimated P\&I}$

* Insurance and taxes typically make up around 30% of a monthly mortgage payment.

Maximum Qualifying for VA

$GMI \times 41\% - \text{debts} = \text{Max PITI}$

See chart for residual family income; # of family members determines the income less debts to equal an amount required for family support.

See www.VA.gov for updated guidelines.

Maximum Qualifying for Department of Agriculture (USDA – Rural Development)

$GMI \times 43\% - \text{debts} = \text{Max PITI}$

Qualifying buyers

Possibly the most important question to ask the borrower is:

“What is the highest monthly payment you are comfortable with?”

For example: Mr. and Mrs. Buyer want a maximum monthly house payment (PITI) not to exceed \$1,800.00.

Step 1: $\$1800 (\text{PITI}) \times 60\% (\text{insurances and taxes}) = \1080.00 (estimated P&I) Multiplying by the 60% isolates the P&I from the expected total payment.

Step 2: $\$1080 / .00599 = \$180,300.00$
(.00599 is the factor for the base loan 6% Rate for 30 years)

Step3: (For FHA w/3.5% down)

$\$180,300 / 96.50\% = \$186,839.00$ (Sales Price).

Check the Math

$\$186,839$ (Sales Price)	$\$186,839$ (Sales Price)
$\times 96.50\%$	$-180,300$ (Base Loan)
$\$180,300$ (Base Loan)	$6,539$ Down payment

Base loan amount: $\$180,300 \times 101.75\% = \$183,455.00$ with Annual Mortgage Default Insurance financed into the loan.

Loan amount: $\$183,455$ (with MIP) $\times .00599 = \$1,098$ P & I

$\$183,455 \times 1.9\% \div 12 = \290 Est. Homeowners

$\$183,455 \times 0.9\% \div 12 = \137 Est. Flood Insurance

Sale price: **\$186,839.00**

Loan application procedures

The steps to home ownership go through the loan application procedures which are fairly common throughout the industry.

1. Prequalification – A lender will generally do some form of prequalification with prospective borrowers
2. Find the property – The buyers will seek out the home they want to purchase
3. Make an offer
4. Complete the loan application – This is much more than filling in a piece of paper.
5. Closing – The last step to seal the deal

Let's take look at each of these steps.

Loan application procedures - Prequalification

The first step in getting a prospective buyer into a home is to get them prequalified (or pre-approved) for a mortgage loan.

Nothing is more frustrating and time consuming than to go through a home search and application process with a client and then find out they don't meet minimum requirements, or can't afford the home they want to buy.

- **Pre-qualified** – The lender makes an estimate of how much a buyer might qualify for based on preliminary calculations. Lenders are not committed to make a loan based on this preliminary estimate.
- **Pre-approved** – Lenders will provide a pre-approval letter after verifying credit, employment and other information. The buyer is not bound to a pre-approval and can ask multiple lenders to provide a pre-approval letter.

Loan application procedures - Find the Property

As a broker or agent you must understand the buyers wants and needs.

Helping that buyer find the right house involves striking a balance between the "must-haves" and the "nice-to-haves." The agent should show properties in various locations that meet the price, property amenities, community and style desires.

The agent should be prepared to walk the buyer all the way through the search process.

Loan application procedures - Make an offer

Once the buyer has settled on a property they should immediately extend an offer to purchase which can have many aspects:

- Price offer – The offer may be well below the listed price if it has been on the market for a long time or higher than the asking price if it's a new listing and the market is hot.
- Contingencies – Is the purchase contingent on other things such as the sale of an existing home or the ability to get a loan at a certain rate.
- Comparables – what are comparable homes in close proximity selling for
- The seller's needs – Does the seller need to move quickly or hasn't received other offers.

There's more to applying for a mortgage loan than filling in a form.

As the agent you should help the buyer understand precisely what he will need to provide to expedite the loan approval process.

- Required documentation
 - Proof of income – This is generally in the way of recent pay stubs and W2 forms, as well as any documents proving other income sources – Social security or disability payments, rental income, alimony or child support, etc...
 - Last two tax returns – Lenders commonly ask for these.
 - Employment history – Lenders will want to know the buyers employment stability.
 - List of assets and debts – a well-rounded view of the buyer's financial standing is crucial. A complete list of assets and liabilities will be needed.
- Source of down payment – There are specific rules regarding gifts used for down-payment. A lender will want to know where the down-payment is coming from.
- Property appraisal – A basic property valuation should be provided.

Loan application procedures - Closing

The closing is the last step in the home buying process.

The closing agent will generally be responsible for preparing or ordering all the documents required for the closing.

You must ensure the buyer is ready for closing and has:

- Homeowners insurance
- Certified check for all closing costs including balance of down-payment.

At the closing the new homeowner will receive several documents many of which will be covered later on in this training.

The things that happen at closing:

- Terms of the agreement between the buyer and the mortgage lender are confirmed.
- The loan goes into effect and the buyer receives his mortgage.
- The terms of the sales contract are confirmed.
- Ownership of the home is transferred.

Types of Real Estate Loans

In this section we will discuss various types of loans available on the mortgage market, including: Term or Straight Loans, Amortized Loans, Adjustable Rate Loans and more.

Term Loans (Straight Loans)

A straight or term loan is characterized by periodic payments of interest, followed by a single lump sum re-payment of the loan principal at the end of the term.

The lump sum due at the term's end is called a balloon note payment.

Term loans are typically for one year periods.

Amortized loans

A fully amortizing loan is characterized by a series of constant or level (annuity) payments over the life of the loan.

The most common of these are the 30 year and 15 year fixed term amortized loans.

A portion of each payment goes toward paying down the loan balance.

The interest paid, as a part of the periodic payment, is highest in the initial periods and declines thereafter.

By the end of the amortization period, the outstanding loan balance will have declined to zero.

Some loans may be only partially amortized with a due date term of 3 to 5 years when the balance comes due – Balloon Payment.

There are cases where a loan may have negative amortization and the payments don't cover the interest accrual.

With each payment the outstanding loan amount increases quickly, driving the loan “underwater.”

Both lenders and borrowers suffer from these lose-lose scenarios.

Adjustable Rate Mortgages (ARM)

Adjustable-rate mortgages (ARMs), have monthly payments that can adjust up and down as interest market rates fluctuate.

Typically, the interest rate is fixed for an initial period and thereafter the rate can change every year.

For example the 5/1 ARM has an introductory term of five years and annual rate changes each year after.

Since rates are based on prevalent market interest rates, the index, it's possible for the payment to go down if the index is lower than it was when the loan was initiated.

Some lenders may offer alternatives such as: 3/1, 7/1 or 10/1 ARMs.

Another factor involved in ARMs are the **caps**, or the allowable amount rates and payments can change.

- A **periodic rate cap** limits how much the interest rate can change from one year to the next.
- A **lifetime rate cap** limits how much the interest rate can rise over the life of the loan.
- A **payment cap** limits the amount the monthly payment can rise over the life of the loan in dollars.

Convertibility is a provision built into an ARM giving the borrower an option to convert the loan to a fixed rate at certain points during the mortgage agreement.

The conversion rate is very often set at a level slightly higher than the market rate existing at the time of conversion.

Borrowers choosing this option are not required to qualify for the new conversion rate.

Conventional vs. Insured

Loans made by lenders can be divided into two main categories:

- Conventional loans
- Government-insured loans

Conventional Loans

Any institutional loan not insured or guaranteed by a government agency is a conventional loan.

- **Conforming loan** - complies with Fannie Mae/Freddie Mac guidelines.
- **Non-conforming loan** - does not comply with Fannie Mae/Freddie Mac guidelines.

Most non-conforming loans are subprime loans

Conventional Conforming Loans

Conventional loan may be secured by:

- Principal residence (up to 4 dwelling units)
- Second home, (no more than 1 dwelling unit)
- Investment property, (borrower doesn't intend to occupy)
- Allowed maximum properties financed (borrower doesn't intend to occupy)

FNMA will allow ownership interest in up to 10 properties with these guidelines:

- 25% down payment on the property
- Minimum credit score of 720
- No mortgage late pays the last 12 months
- No bankruptcies or foreclosures in the last 7 years
- 2 years of tax returns showing rental income from all rental properties
- 6 months of PITI reserves on each financed property

Loan Amounts – Conforming loan limits are set annually by Fannie Mae and Freddie Mac

- Agencies won't purchase loan if it exceeds limit
- Different loan limits for different parts of U.S.

Jumbo loan - loan that exceeds conforming loan limits. Extra-large loans are sometimes called super jumbos.

- About half of jumbo loans are ARMs
- Higher interest rates

Conventional Conforming Loans

Conventional Conforming Loans

Common conventional LTVs: 80%, 90%, 95%

Less common conventional LTVs: 97% & 100%

Conventional loans are often categorized by LTV ratio, with different underwriting rules applied to each category

Fannie Mae and Freddie Mac require private mortgage insurance for any conventional loan with LTV over 80%

High-LTV loans also have:

- Higher interest rates and fees
- Stricter underwriting rules

If certain conditions are met both Fannie Mae and Freddie Mac are willing to buy ARMs with LTVs up to 95%

Make sure you understand all aspects of conventional financing as you support your agents and their clients.

Government Insured Loans

Brokers/agents will typically deal with three Government backed loans on a regular basis.

- FHA-insured loan program
- VA- guaranteed loan program
- USDA Rural-insured loan program

Government Insured Loans - FHA

The Federal Housing Administration (FHA) was created in 1934 as part of National Housing Act to:

- Generate new jobs by increasing construction activity
- Stabilize mortgage market
- Promote financing, repair, improvement, and sale of real estate

Distinguishing features of FHA loans:

- Less stringent qualifying standards.
- Borrowers with minimum decision credit score at or above 580 are eligible for maximum financing.
 - 3.5% down payment
- Borrowers with minimum credit score between 500 and 579 – limited to 90% LTV.
- Borrowers with minimum credit score of less than 500 are not eligible for FHA-insured financing.
- Secondary financing restrictions.
- Maximum loan amounts set by local limits and by LTV rules.
- Borrower must come up with min cash investment plus funds for closing costs, discount points and prepays.
- Mortgage insurance always required.
- No pre-payment charges.
- Property must be owner-occupied primary residence.

Government Guaranteed Loans - VA

The VA loan program was established to help veterans finance the purchase of their homes and offers many advantages over conventional financing.

VA-guaranteed loans are made by institutional lenders, but a portion of loan is guaranteed by Department of Veterans Affairs and protects lender against losses from default.

May be used for finance, purchase or construction of a one-to-four unit residences.

- Does not guaranty investor loans
- Veteran must occupy home

Key characteristics of VA loans:

- No down payment required
- No maximum loan amount
- No maximum income limits
- Least stringent qualifying standards
- Can be fixed-rate or ARM loans
- No mortgage insurance required

- No maximum interest rate
- Lender may charge flat fee of no more than 1% for administrative costs
- No prepayment penalties
- Forbearance extended to veterans with financial difficulties
- Can be assumed by creditworthy buyer, veteran or non-veteran

Government Insured Loans – USDA Rural

Provides homeownership opportunities to rural Americans.

- Includes home renovations
- Also programs for the elderly, disabled or low-income of multi-unit housing buildings

Highlights of USDA Loans:

- 100% Financing
- Broad location guidelines
- No mortgage insurance requirement
- No seller contribution limit
- 100% of closing costs can be gift
- Loan amount can include closing costs and repairs up to a/v

Reverse Mortgage – Sometimes referred to as a Home Equity Conversion Mortgage (HECM)

Allows older homeowners to convert equity into a monthly source or line of credit:

- Both borrowers must be 62 years old.
- Must own the property outright or paid down a considerable amount.
- Occupy the property as a principal residence
- Not be delinquent on any federal debt.
- Participate in a consumer information session given by a HUD-approved HECM counselor.

Refer to HUD for specific HECM for homeowner and property requirements.

Homeowners can draw cash from their equity a couple of ways:

- Home Equity Line of Credit (HELOC) – This is a line of credit setup with your home equity as collateral. You are able to draw cash as needed/when needed up to the limit of the loan. Typically these are adjustable loans. The payment amount will fluctuate with the market.
- Equity loan – Essentially a second mortgage where the rate is usually fixed and you repay both interest and principal each month. The payment is received as a lump sum and you cannot draw additional money from the loan. The interest rates are generally higher than HELOCs of the same amount.

Sub Prime and Other Nonconforming Loans

Subprime lending involves making riskier loans:

- A credit = Prime or standard financing
- A- to B, C, D credit = Subprime financing

Subprime lending may involve:

- Poor credit rating
- Lack of documentation
- High debt ratio
- Nonstandard property
- Large loan amount
 - Jumbo
 - Super Jumbo

Subprime lenders often engage in predatory lending practices and commonly feature:

- Higher interest rates
- Higher loan fees
- Prepayment penalties
- Balloon payments
- Negative amortization

Secondary subprime markets grew in '90s.

The subprime boom ended in the late '90s when the default rate rose and most subprime lenders went out of business.

Subprime lending is currently making a resurgence in the home mortgage marketplace.

Other non-conforming loans:

- Jumbo or Super Jumbo loans – Jumbo mortgages are home loans that exceed conforming loan limits and is used primarily to buy a high-priced or luxury home.
- Interest only loans – The borrower only pays the interest on the mortgage through monthly payments for a term that is fixed, usually between 5 and 7 years). It lets the buyer get more home for the same payment. Interest only loans should not be considered for buyers intending to stay in the home long-term.
- “Payment Option” ARMs – In this option the borrower can choose between several monthly payment options with payment calculated based on the initial temporary start interest rate. This is a very risky loan with the high probability of negative amortization should the index go high and the borrower is making minimum payments.

Sources of Loan Money

In this section we'll take a look at where mortgage loan money can be found.

- Seller/Owner Financing
- Primary Market
- Secondary Market
- Down Payment Assistance

Seller/Owner Financing

Sometimes the seller will take on the role of lender and provide property financing.

Instead of giving cash to the buyer, the seller extends enough credit to the buyer for the purchase price of the home, minus any down payment. The property is the collateral. If the buyer fails to make the required payments property ownership reverts back to the seller.

Usually the loans are short term. For example - The loan might be amortized over 30 years but has a balloon payment due in five years.

The assumption is, the home will have gained enough in value or the buyers' financial situation will have improved enough that they can refinance with a traditional lender when the balloon comes due..

Sellers would usually require a loan application just like any traditional lender. Loan approval would be a contingency of sale.

Primary Market

Banks, credit unions, mortgage brokers and bankers all make up the primary market.

These are typically local institutions who loan directly to the consumer.

Advantages of a primary lender:

- **Local market knowledge** – Because primary lenders more often are in the community they can move swiftly to approve loans.
- **Flexible** – Primary lenders have the flexibility to arrange loan terms to fit varying circumstances where other out-of-market lenders might not.
- **Lower closing costs** – Because primary lenders do their own underwriting many of the closing costs can be reduced – secondary market fees, which can be burdensome, are not in play. Some primary lenders may not require insurance and taxes to be escrowed.

Disadvantages of primary lenders:

- ARMs are the preferred loan type of primary lenders.
- Down payments normally 10% or more.

Secondary Market

Fannie Mae, Freddie Mac and Ginnie Mae are the key players in the secondary market.

These organizations buy mortgages, usually originated through mortgage brokers, or some of the larger regional and national banks. They have very strict guidelines that must be met for them to purchase these loans from the originator. They never see the buyer or the property.

Advantages of the secondary market:

- **Fixed rates** – While increases in taxes and insurance could cause your payment to rise during the course of the loan, with a fixed rate loan the principal and interest remains fixed over the life of the loan.
- **More down payment options** – Some borrowers will qualify for loans with little or no down payment using the government backed programs, FHA, VA, USDA and others.

Disadvantages of the secondary market:

- **Escrow** – Normally secondary market borrowers must escrow insurance and taxes to cover six months of property taxes and one year of insurance. Once the borrower has 20% equity in the property this can be waived.
- **Private Mortgage Insurance (PMI)** – Borrowers with less than 20% equity in their home are required to pay PMI on top of their normal payment.
- **Closing costs** – Secondary market loans usually come loaded with fees not found with primary lenders. These can include underwriting fees, application fees, document preparation fees, inspection fees, and many more.

Down Payment Assistance Programs

Reaching out for the American Dream of homeownership sometimes requires a little help getting there.

Some of the government backed programs such as FHA and VA already have some reduced down payment options, but sometimes more help is needed.

Credit/Financing Laws

There are many rules and regulations regarding consumer and commercial credit. In this lesson we will take a high level look at some of those regulations, such as: Truth in Lending, RESPA, Equal Opportunity Credit, Mortgage Loan disclosures and more. For the purpose of this lesson we will focus on the general requirements and practical application of the rules.

Truth in Lending Act (TILA)

The Truth in Lending Act (TILA) of 1968 is implemented by Federal Reserve Board's Regulation Z.

The primary purpose of TILA is to:

- Regulate disclosure of finance charges
- Show the estimated total costs of borrowing, the expected payment amounts over the life of the loan, and other significant loan features.

The application of this regulation, by an individual or business entity, should be adhered to when the following conditions are met:

- When offering or extending credit to consumers on a regular basis.
- Finance charge is attached to this credit or is payable in more than four monthly installments per a written agreement.
- Credit is primarily for personal, family, or household purposes.

The Truth in Lending Act only applies to loans made to natural persons and does not apply to:

- Loans made to corporations or organizations
- Loans made for business, commercial, or agricultural purposes
- Loans > \$25,000 not secured by real property
- Seller financing

Refer to the Sample Disclosure form downloaded at the beginning of this course for example TILA disclosures.

Real Estate Settlement Procedures Act – RESPA

RESPA was passed in 1974 with two main goals:

- To provide borrowers with information about closing costs
- To eliminate kickbacks and referral fees that unnecessarily increase settlement costs.

An in-depth examination of RESPA can be found at: www.hud.gov/respa

RESPA is divided into two groupings:

- One section manages disclosures and servicing requirements for transactions involving a “federally related residential loan”.
- The second set prohibits the payment or receipts of fees from the borrower that were not actually earned.

RESPA applies to "federally related" loan transactions.

A loan is federally related if it is secured by a mortgage or deed of trust against:

- Property with (or money will be used to build) dwelling of four units or less:
- Condominium or cooperative apartment
- Lot with a mobile home
- Lender is federally regulated – Which means that the lender has federally insured accounts, is assisted by federal government, makes loans in connection with federal program, sells loans to Fannie Mae, Ginnie Mae, or Freddie Mac, or makes real estate loans that total more than \$1,000,000 per year.

RESPA will not apply to loans:

- To purchase 25 acres or more
- Business, commercial, or agricultural purpose
- To purchase vacant land – unless within two years from the loan settlement date, a structure or a manufactured home will be constructed or placed on the real property using the loan proceeds.
- Temporary financing (construction loan)
- Assumption without lender approval

Equal Credit Opportunity Act – ECOA

The Equal Credit Opportunity Act (ECOA), Regulation B, was passed in 1974 and applies to all consumer credit.

The definition of consumer credit under the ECOA is:

Credit extended to an individual for personal, family, or household purposes.

The purpose of the ECOA is to promote the availability of credit to all creditworthy applicants without regard to race, color, religion, national origin, sex, marital status, or age.

The ECOA requires lending institutions and mortgage brokers to perform specific actions and applies to anyone involved in granting credit:

- Real Estate Brokers who arrange financing
- Small loan and finance companies
- Retail and department stores
- Credit card companies
- Credit unions

A full description of the ECOA requirements can be found at: www.consumer.ftc.gov

Mortgage Loan Disclosures

RESPA requires lenders provide specific mortgage loan disclosures at various stages of every loan transaction:

Within three (3) business days of application:

- HUD's Settlement Cost Booklet – Provides information to help borrowers understand the home-buying and mortgage process so that they make informed decisions and avoid common problems.
- Good Faith Estimate – The estimate must include an itemized list of fees and costs associated with the loan.
- Mortgage servicing disclosure statement – Discloses to the borrower whether the lender intends to service the loan or transfer it to another lender.

Mortgage Loan Disclosures

RESPA requires lenders provide specific mortgage loan disclosures at various stages of every loan transaction:

Before closing:

- Affiliated arrangement disclosure – This is a disclosure that reveals what, if any, business relationship exists between the Mortgage Broker and the lender, including what fees are charged due to the relationship.
- HUD-1 settlement statement – This is a statement of the loan transactions fees that would be paid by the buyer and seller at closing.

At closing:

- Final HUD-1 settlement statement
- Initial escrow statement

Each year the buyer should receive an annual escrow statement showing how much was paid into the account and how much your lender paid out in taxes on the homeowner's behalf.

Good Faith Estimate - GFE

The GFE is an estimate of the likely settlement costs.

Look for the HUD Good Faith Estimate form you should have downloaded before starting this lesson and follow along.

Some key sections of this form are:

Page 1

- Important dates
- Loan Summary
- Escrow account

Page 2

- Origination and Settlement charges

Page 3

- Trade-off table
- Shopping cart

Closing Disclosure Requirements

The Closing Disclosure form is a statement of the final loan terms and closing costs. The requirements are:

- Closing disclosure must contain the actual terms and costs of the loan.
- The closing disclosure must be in writing and contain the information prescribed in §1026.38.
- Creditors must provide the closing disclosure three business days before consummation.
- Creditors must use form H-25 for any federally related mortgage loan.

Many of the TILA-RESPA requirements changed including the closing disclosure form in 2015. Take the time to go through the TILA-RESPA Integrated Disclosure rule guidelines put out by the Consumer Financial Protection Bureau and provided in the download area for this lesson.

REAL ESTATE CALCULATIONS

OBJECTIVES

As a real estate professional, your constant companion will be your financial calculator. Mathematics is a huge part of the job. You and your agents must be proficient with the various real estate calculations performed on a regular basis. From basic math to advanced area and percentage calculations you must be proficient across the board. Upon completion of this lesson, you should understand:

1. General Math Concepts
2. Calculating property tax
3. Other transactional calculations
4. Mortgage calculations

General Math Concepts

In this section we're going to start at ground level and go through some very basic math fundamentals: Addition, subtraction, multiplication, and division. We'll cover percentages, decimals and fractions, and wrap up with an overview of how to calculate areas, by acreage.

Addition is the process of calculating the total of two or more numbers or amounts.

For example – Say you have an investor that owns four houses.

He buys one more,.... now how many does he own?

That's right..... Five. Our investor now owns five houses

So if we run that same math on our calculator

ONE ...PLUS ... FOUREQUALS FIVE

Adding numbers in real estate will usually involve much larger numbers. It's important to understand number value and structure.

For example, if you want to add several numbers together, such as:

$1,378 + 475 + 321$, you'd have to understand the values of each digit to come up with the sum. So let's look at the structure of the first number 1,378.

The numbers to the right tell us how many ones are in the sum of this number. The next number to the left tells us how many tens are represented, then how many one hundreds, then thousands and so on and so on for as many places as you take the number to the left.

So if we add up those values we get:

Eight ones = 8

Seven tens = 70

Three hundreds = 300

And one thousand = one thousand

Reading from left to right we can now say, one thousand, three hundred and seventy eight.

So now knowing that, let's sum our three numbers. We do that one column at a time. First, the ones.

We have $8 + 5 + 1 = 14$

Right now we are only dealing with ones, but now we have 14 (that's 10 plus four). Let's move that ten up above the ten column so we can add that with the tens.

Now add $1 + 7 + 7 + 2$ That equals 17.

Now we've got too many tens. We know ten tens is a hundred so let's move that over to the 100 column and keep the seven in place.

Now let's add the 100s. $1 + 3 + 4 + 3 = 11$ hundreds

Same thing... we know 10 hundreds is 1,000 so let's move that over into the 1,000 column and do that math.

$1 + 1 = 2$ thousands.

So the sum of these three numbers is two thousand, one hundred and seventy four. Let's verify that with the calculator.

On our calculator enter 1-3-7-8 plus 4-7-5 plus.

You will notice that entering the second "plus" subtotals your math to that point. $1378 + 475 = 1853$.

Continuing on enter 3-2-1 plus and then press equals. That totals out the math.

Subtraction – The process of finding the difference between two numbers or quantities.

For example let's revisit our investor. Since we last visited our real estate mogul he has increased his property ownership to eight houses.

Our investor put four of these on the market for sale.

Sometime later three of them sold.

How many does he have left. That's correct....– Our investor still owns five house.

To confirm that let's run it through our calculator...

Eight minus three equals five.

The process for subtracting larger numbers is the same column concept used in the addition slide. You would subtract each column individually.

So first do the ones column $8 - 2 = 6$

Then do the tens column $2 - 1 = 1$

The result is: 16

To verify that on the calculator it you would press

$2 - 8$ minus $1 - 2$ equals.

You will run into situations where you have to be a "borrow" from the left column because your top number is smaller than your bottom number.

For example in the equation 24 minus 17,

...looking at the ones column you'll see the four is smaller than the seven.

If you borrowed a ten from the ten column and added it to the ones column, now you can do the subtraction: 14 minus $7 = 7$.

Because you borrowed the ten, now you are left with $1 - 1 =$ zero. so the solution is $24 - 17 = 7$

Multiplication – In simple terms, multiplication is adding the same number together multiple times.

Checking in with our investor, we find out he is planning to purchase two houses a month for six months. At the end of six months, how many houses will he have purchased?

The multiplication equation is: 2 houses times 6 months.

A simple way to look at it would be 2 added together six times.

Or 2 6s added together

The answer is 12 houses.

Let's confirm that by watching the investor start buying houses in January and see how many he has by the end of June.

In the graphic we see in fact that the investor has purchased 12 houses in 6 months.

Let's prove that by following along on your calculator.

Two times six equals twelve.

With larger numbers it gets a bit more cumbersome but can still be simple if you follow the procedure.

You end up doing the math separately on each number like this.

Let's do the ones side of the number first ... $782 \text{ times } 6 = 4,692$.

Follow along with your calculator as shown.

Then you go do the tens column . 9 times 782 = 7,038.

Since the nine was in the second position make sure you shift the result to the left to account for this.

Then you sum those numbers to get the result of the equation. Check the result on your calculator as shown.

Division – The action of separating something into parts, or the process of being separated.

Consider this example.

An apartment building has eighteen apartments total. There are three apartments on each floor with none on the first floor. How many floors are there above the lobby?

We could look up and count floors or we could solve it easily by using division.

The question in math terms is how many groups of three are there among 18 apartments?

The math statement is 18 apartments divided by three apartments on each floor is six floors.

Let's confirm that on the calculator – 18 divided by 3 = 6.

Let's consider the numbers in the equation 234 divided by 71 and describe each individually.

495 is the dividend – the number to be divided into.

23 is the divisor – the number we will divide into 495.

The answer to the equation is the result.

Manually dividing large numbers can get quite cumbersome. Using a calculator is always the preferred method. We have provided a long division solution to this problem in your resources download titled "Long Division Solution.pdf". Take a moment to look that over and it becomes quite evident of why you want to use a calculator. It's just too easy to make errors.

So let's plug those numbers into our calculator and see what we get.

4 9 5 divided by 23 equals 21.52

And on and on and on.... This gets us into the world of decimals and fractions which will be covered in the next section of this lesson.

In this next section we'll discuss fractions and decimals - numbers with a value less than 1, and percentages, an amount that is a proportion of a larger number.

For example, the slice of pie in the image below, highlighted by the white chalk fill represents 25% of the whole pie.

A fraction is nothing more than a smaller part of a whole something – For our example the whole something is a "Whole square mile."

Let's say we want to break this property into four pieces.

Now we have created four squares out of our one square mile.

So our first example of a fraction is each of those squares is one-half mile square.

But each square also represents one-fourth of a square mile.

The top number of the fraction is the NUMERATOR. It represents the number of parts you have here. In the case of our example, that's "1" half mile square.

The bottom number is the denominator. It represents how many parts the whole is divided into. In this case, "4" one-half mile squares.

To add these fractions together you would simply total the numerator and leave the denominator alone since it already totals the whole.

$$\text{One fourth} + \text{One fourth} + \text{One fourth} + \text{One fourth} = \text{four-fourths}$$

When the numerator and the denominator are the same, this is equal to the whole. You prove that by dividing the denominator into the numerator.

$$4 \div 4 = 1$$

To this point we've talked about each half-mile quadrant being one-fourth of the square mile. So what happens if we divide the numerator by the denominator?

$$1 \div 4 = .25$$

The smaller parts of the whole can also be shown as a decimal, in this case 0.25.

Verify that with your calculator.

We'll expand on decimal values and show the relationship to percentages later in this lesson but first let's carry fractions out a little further.

In this example we want to split our one square mile property into eight equal sections, one quarter mile in width and one half mile in depth. When complete that would look like this.

Each section would represent one-eighth of a square mile.

Suppose three of these sections were grouped together and sold off as a piece of property.

What fraction of the square mile would that be?

We can solve that easily by simply adding the numerators together.

$$\frac{1}{8} + \frac{1}{8} + \frac{1}{8} = \frac{3}{8}$$

To convert the three-eighths fraction to a decimal, divide the numerator by the denominator ... $3 \div 8 = 0.375$

Prove that on your calculator by entering $3 \div 8$ and the result would be 0.375

Knowing that we've sold off three-eighths of our square mile, how much property do we have left as a fraction of the whole? We can solve that very easily with simple fraction math.

We use the same concept to subtract fractions as we do when we add fractions, except we start with the whole written as a fraction.

$$\frac{8}{8} - \frac{3}{8} = \frac{5}{8}$$

Now convert that five-eighths to a decimal by dividing five by eight.

.625

Use your calculator to confirm the answer.

Recall that we have subdivided our property into essentially two pieces representing .375 and .625 of a square mile.

Plug that into your calculator and confirm.

Point three seven five plus

Point six two five equals one

To break this into percentages a basic understanding of what percentages are will be necessary. We'll come back to this shortly.

A **Percentage** just means per 100.

So let's divide our square mile into 100 sections.

Each section would then be one tenth of a mile in both width and depth

But as a percentage of the whole each section would be 1% (or one-one hundredths) of the square mile.

In decimal terms that's .01.

Let's prove that using the calculator and what we learned before about fractions.

$$1 \div 100 = .01$$

Looking back to our .375 and .625 slices of our square mile, let's see how easy it is to convert a decimal to a percentage. You simply shift the decimal place to the right twice.

SO .375 becomes 37.5 and .625 becomes 62.5

The 37.5% represents thirty-five (35) whole sections

and five (5) half sections.

You can prove that by adding all the sections together. Thirty-five whole sections plus five half-sections = thirty-seven point five.

That concludes our over view of basic math, fractions, decimals and percentages. Before moving on to the rest of the lesson, we'll take a look at calculating areas.

For this discussion we'll stay with our square mile example but relate that to equivalent acres. For visualization purposes consider that an acre is a bit less than a football field.

We know one square mile is 640 acres, so we can subdivide that into 100 sections by dividing 640 by 100.

So we now know that 1% of a square mile represents 6.4 acres.

The acreage you will normally be calculating will be related to lot size. Let's take a look at how to calculate area of different shapes.

An acre is a measure of area and is not defined by length or width. An acre can be of any shape – a rectangle, a triangle, a circle, a trapezoid or any other shape—so long as its area is exactly 43,560 square feet.

See what happens when a contractor builds the same size house on lots of various acreage. The house on the one acre lot looks tiny when built on one acre.

The acre was originally an English unit of measurement that described the area that a yoke of oxen could plow in a day.

It originally differed in size from one area to the next, but was ultimately fixed at 4,840 square yards, or 160 square chains (its current size).

The most common acre shape is 660 feet by 66 feet – “One furlong” by “One chain”.

Defining an acre square is pretty simple. In math terms the “square root” of a number is: The number to multiply by itself to find the original number.

For example we intuitively know that $3 \times 3 = 9$ so the square root of 9 is 3.

But how do we find the square root for such a large number?

Tip: Let your calculator do it.

So if you have a very basic calculator that doesn't have a Square Root function, it is highly recommended that you get one shortly.

To find the square root using your calculator you enter the number followed by the square root key and it will display the square root.

Four-three-five-six-zero – Square root and the result is 28.71 etc... I usually round off to the nearest tenth or the first digit to the right of the decimal.

Calculating acreage on odd sized lot

Suppose you have a lot that is not a square or a rectangle. It might be longer on one side than the other. For example:

Here's a piece of property that is 345 feet along the front edge and 275 feet along the back edge. The property is 280 feet deep.

We also know the center line of the property is aligned along the front and back. This gives us everything we know to calculate the acreage.

First let's find out the square footage within the 275' center section.

That's simple math – 275 feet times 280 feet equals 77,000 square feet.

Then we can find out the acreage by dividing the sq footage by the 43,560 number. The result is 1.76 acres. Now we just have to calculate the area of the triangle sides. .

Subtracting 275 from 345 tells us there is 70 linear feet less on the back than the front. Since that's the same on each side we can use 35' in our calculation.

To calculate the area of a triangle we can use the following formula.

$$\begin{array}{rcl} \text{Area} & = & \frac{1}{2} \times b \times h \\ b & = & \text{base} \\ h & = & \text{height} \end{array}$$

To find the area of each property triangle, the math is:

$$.5 \times 35' \times 280' = 4,900 \text{ square feet}$$

$$\text{To find acreage we would divide } 4,900 \text{ by } 43,560 = .112 \text{ acre}$$

Now all we have to do to find total acreage is add the .112 acres twice, one for each side of the property, into our previous calculation. We'll just round that off to .11.

We had 1.76 acres and to that we'll add .11 twice and come up with a total of 1.98 acres.

In real estate you will use math of various levels of complexity on an almost daily basis. A small error, a shifted decimal, or a missed number somewhere can relate to thousands of dollars in miscalculations. Your constant companion should be your calculator and the skill to use it.

A good practice to develop is to always double-check your calculations. Prudence demands it.

Property Tax Calculations

In this section we'll do a brief overview of how property taxes are calculated.

The four main components to the calculation – assessed value, assessment rate, exemptions and tax rate will be needed for the calculation.

Calculating property taxes in Louisiana follows the same fundamental processes found in other states. Although the calculation is essentially the same, the tax bill on equitable properties could vary substantially across different Parishes, municipalities and school districts in Louisiana. The basic formula is:

$$((\text{Assessed Value} \times \text{Assessment Rate}) - \text{Exemptions}) \times \text{Property Tax Rate} = \text{Tax Bill.}$$

For comparison consider that St. Tammany Parish historically collects the highest property tax in Louisiana with an average of 0.66% of median home value, where St. Landry Parish levies the lowest property taxes in the state, collecting an average of only 0.25% of median home value annually.

Since we will be discussing the specifics of valuation, appraisal and pricing in the next lesson, we'll use general terms to talk about property valuation here.

The Tax Assessor of the Parish where the property is located is responsible for an annual property appraisal. That will give us the first number, the assessed value, necessary for our property tax calculation.

The appraisal is based on the features of the property and the fair market value of comparable properties in the same neighborhood.

For our property tax example we are going to look at a property in the Highland Park area of Shreveport that has an appraised value of \$200,000.

The land is appraised at \$42,000 and the residence at \$158,000.

Now we can plug that \$200,000 assessed value into our calculation.

In Louisiana the classification of property subject to ad valorem taxation and the percentage of fair market value applicable to each classification for the purpose of determining assessed value is as follows:

Classifications	Percentages
1. Land	10%
2. Improvements for Residences	10%
3. Improvements for Commercial	15%
4. Business Movable Property(Personal)	15%
5. Public Service(excluding land)	25%

Since both land and residence are both assessed at 10% we can plug 10% into our formula as shown.

We know 10% is also 0.1 so multiplying \$200,000 x 0.1 we get a taxable value of \$20,000.

We'll come back to exemptions in a little bit, but first we'll establish the tax bill without any exemptions.

Tax rates are based on "Mill Rates" which vary around the different parishes and municipalities throughout the state.

A mill is defined as 1/10 of 1 percent and is multiplied by the assessed value after any exemptions have been subtracted to calculate the taxes.

For example, If the total assessed value is \$10,000 with no exemptions, and the tax rate is 150 mills, the taxes would be calculated as $\$10,000 \times .150 = \1500.00 .

At the Parish Tax Assessor's website you should find the current millage rates corresponding to the location of the property.

For Caddo Parish, this is the Mill Rate table. So we see here that the Mill Rate for the Parish, including the towns of Shreveport, Vivian and Bossier city is 130.59. You can see in the table that each operational entity within the Parish calculates its required mill levy and then all are tallied up to equal the total mill levy.

We also know that the Highland Park area of Shreveport falls within the municipality and gets an additional tax.

Parish wide tax: 130.59 mills + 39.70 mills = 170.29 mills is the total tax rate for this property.

Assuming there were no available exemptions for our Shreveport property the tax bill is \$ 3,405.80

Exemptions could have a significant impact on the tax bill.

For example, the homestead exemption states:

"... the property in indivision shall be exempt from state, parish, and special ad valorem taxes to the extent of **seven thousand five hundred dollars** of the assessed valuation."

So when we deduct the \$7,500 Homestead Exemption from our assessed value we get \$12,500. Multiply that by the mill rate and the new tax bill is \$ 2,128.62, nearly \$1,300 less than without the exemption.

The subject of exemptions from property tax is extensive and outside the purpose of this training. However you will find the core text of the statutes regarding taxation and exemptions as a handout. Questions regarding exemption on a specific piece of property should be addressed to the Tax Assessor of record in the Parish where the property is located.

Other transaction calculations

Real estate brokers and agents are always having to calculate something. Some of the other transactions you will come across regularly are: Prorations (Property taxes, mortgage insurance, rent, utilities, etc.) expenses that would be split between the buyer and the seller, Seller's proceeds of sales, the total cash the buyer will need at closing and any other conveyance taxes required.

Proration – Property Tax

The Buyer and Seller normally agree to prorate the cost of any expenses related to the property that may be due in the year of the sale, e.g., taxes, homeowner's association dues and condominium association dues, rent, utilities.

These are covered on line 90 of the residential purchase agreement and should be clearly explained to the buyer and seller so there are no surprises at the closing.

Taxes are easy to prorate because in Louisiana they are due on December 31st.

Consider this scenario:

If the closing is on January 30th the Seller will hand over to the Buyer 30 day's worth of taxes so that at the end of the year, the next following December 31st the Buyer will have 1/12th of the year's taxes, and he is liable for the balance.

(Annual tax bill ÷ 365 = Daily tax bill)

Let's assume for this example the annual taxes are \$2,500.

(\$2,500 ÷ 365 = \$6.85 per day) x 30 days = \$ 205.50

The seller will give the buyer \$205.50 at closing as his prorated share of the annual taxes.

Proration – Mortgage Interest

Mortgage interest is paid in arrears. For a mortgage payment on July 1st, the interest paid is for June.

For the closing you have to calculate the buyer and seller's share of the interest prorated to the closing date.

Let's look at an example where the closing date is July 15th.

The buyer will owe 16 days of interest at closing for July 16 through July 31, since his first mortgage payment will be on September 1 and only include August's interest. The interest proration formula is:

Loan Amount x Interest Rate = Annual Interest (in this case assume \$7,000 annual interest.)

Annual Interest ÷ by 365 days = Daily Interest (7,000 divided by 365 = \$19.18) daily

Daily Interest x 16 Days = Interest Debit Proration

\$ 19.18 daily interest x 16 days = \$306.88

Our buyer will owe \$306.88 at closing for the prorated mortgage interest.

Proration – Rent

Rents are normally paid in advance. Investment property buyers expect to receive a credit for rents received for the dates the buyer owns the property.

A sale that closes on July 15, involving a tenant-occupied property that rents for \$1,500 a month.

The buyer should receive a credit for 15 days of prepaid rent or \$750. The seller would receive a debit of \$750.

Any security deposits should be transferred to the buyer as a credit and a debit to the seller.

Other Prorations

Although rare, in some case you may have to calculate any prorations to be applied to utilities paid by the seller and assumed by the buyer.

HOA fees would also be subject to proration.

The same principal of splitting at the closing date applies in all cases.

Sellers Proceeds of Sale

The money the seller takes away from selling their home after deducting all costs of sale. The calculations look like:

Property Sale Price	\$ 200,000
Less Mortgage Balance	80,000
Less other encumbrances	10,000
Total Estimated Equity	\$ 110,000

Then you would calculate closing costs which might include: Document prep fees, Taxes, Inspection fees, Transaction fees, points to be paid, commissions and any other fees due at closing.	
Total Estimated Deductions	\$ 15,000

Subtract closing costs from equity

Sellers Proceeds of Sale	\$ 95,000
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There are several online forms and calculators to help with calculating proceeds of sales.

Cash required of Buyer at Closing

The buyer will be responsible for paying the down payment and all other accumulated fees at closing:

One-time closing costs and fees: Let's assume for this example these totaled \$ 2,485

These are for things like:

- Origination charges
- Appraisal fees
- Credit report fee
- Title search and Insurance
- Home inspection
- Other seller paid fees

Keep in mind that who pays what fees could be negotiated before closing so these might change dramatically from sale to sale.

Escrow and Prepays: In this case the total is \$ 6,147

These are for things like:

- Escrow property taxes
- Prepaid interest
- Prepaid Homeowners insurance and any other Prorated items.

Those are added together to get a total.

You would then add the down payment.

In our example the buyer would need \$ 27,132 at closing.

Conveyance Taxes

In Louisiana, voters approved an amendment to the constitution in 2011 banning real estate transfer taxes in the state with the exception of Orleans Parish which levies a \$325 fee on any home, business or land sale.

Should you have any questions regarding transfer fees or taxes refer to the Tax Assessor of the parish where the property is located.

Mortgage Calculations

Calculations for mortgage will be common place in your day to day operation. It's important to grasp these concepts. A missed calculation can be costly.

In this section we'll cover down payments, amortization, interest rates and amounts and Monthly payments PITI.

Down payment and financed amount

In most cases buyers are required to make down payments to purchase a home.

Down payments can range from as little as 3% to as much as 20% or higher.

For example, let's assume you want to purchase a \$ 200,000 home. The lender is asking for 10% down.

What is the down payment?

$$\text{\$ } 200,000 \times 10\% = \text{\$ } 20,000$$

So the buyer's mortgage would include \$180,000 for the home. The payment would be based on the interest rate and the term of the loan.

Amortization

An amortized loan schedules monthly payments of both principal and interest across a fixed number of years, usually 15, 20 or 30 years.

Consider this example of a \$100,000, 15-year fixed mortgage at 3.0%.

The first payment of \$690.58 is November of 2015.

DATE	PAYMENT	PRINCIPAL	INTEREST	TOTAL INT	LOAN BALANCE
Nov. 2015	\$690.58	\$440.58	\$250.00	\$250.00	\$99,559.42
Nov. 2016	\$690.58	\$453.98	\$236.60	\$3,163.29	\$94,185.73
Nov. 2020	\$690.58	\$511.79	\$178.79	\$13,131.54	\$71,006.06
Dec. 2025	\$690.58	\$595.99	\$94.59	\$21,492.97	\$37,242.01
Oct. 2030	\$690.58	\$688.86	\$1.72	\$24,304.70	\$0.00

Over a 15-year period the buyer would make 180 payments. Each payment would apply slightly more to the principal and slightly less to the interest because the loan balance decreases each month.

In this example you can see how that is the case and how the interest stacks up over the 15-year term.

What happens to our example of the buyer secures a thirty-year mortgage for the same \$100,000 home?

Monthly payments are less but life-of-loan interest doubles.

DATE	PAYMENT	PRINCIPAL	INTEREST	TOTAL INT	LOAN BALANCE
Nov. 2015	\$421.60	\$171.60	\$250.00	\$250.00	\$99,828.40
Nov. 2020	\$421.60	\$199.34	\$222.27	\$14,424.87	\$88,707.03
Nov. 2025	\$421.60	\$231.55	\$190.05	\$26,802.34	\$75,788.25
Nov. 2030	\$421.60	\$268.98	\$152.63	\$37,091.92	\$60,781.59
Nov. 2035	\$421.60	\$312.45	\$109.16	\$44,956.18	\$43,349.60
Nov. 2040	\$421.60	\$362.95	\$58.66	\$50,003.13	\$23,100.31
Oct. 2045	\$421.60	\$420.55	\$1.05	\$51,777.45	\$0.00

Interest Rates and Amounts

Interest rates can dramatically impact what a buyer pays for a property over the life of the loan.

What if the rate on our \$100,000 mortgage was more than 3.0%?

Remember our payment was \$421.60 @ 3.0%, so you can see in the table how slight increases in the rate increases the monthly payment and the total interest over the life of the mortgage.

RATE %	PAYMENT	TOTAL INT	DIFFERENCE
3.25	\$ 435.21	\$ 56,674.27	\$ 4,896.82
3.5	\$ 449.04	\$ 61,656.09	\$ 9,878.64
4.0	\$ 477.42	\$ 71,869.51	\$ 20,092.06
4.5	\$ 506.69	\$ 82,406.71	\$ 30,629.26
5.0	\$ 536.82	\$ 93,255.78	\$ 41,478.33
5.5	\$ 567.79	\$ 104,404.04	\$ 52,626.59

Monthly Installment Payments (PITI)

PITI is an acronym for a mortgage payment that is the sum of monthly **P**rincipal, **I**nterest, **T**axes, and **I**nsurance.

PITI is the sum of the monthly loan service (principal and interest) plus the monthly property tax payment, homeowner's insurance premium, and, where applicable, mortgage insurance premium and HOA fees.

PRICING AND VALUATION

OBJECTIVES

Pricing and property value is a huge component of any real estate sale or purchase. As a broker you must ensure your clients are getting what they are paying for or pricing their property appropriately for sale. Property priced correctly based on Comparative Market Analysis, value and condition, is essential.

In this lesson we will look at all aspects of valuation and pricing.

Upon completion of this lesson, you should understand:

1. Comparative Market Analysis
2. Broker Price Opinion
3. Valuation by Certified Appraiser

Definitions

Comparable Sale: The sale of a similar property to the subject used for comparison in the valuation/pricing process. All sales are not considered comparable sales.

Comparable Listing: The listing for sale or for lease of a similar property to the subject used for comparison in the valuation/pricing process.

Comparative Analysis: This is the process by which a value indication is derived by analyzing comparable sales. The comparison may be done as a quantitative analysis or a qualitative analysis.

A **quantitative analysis** is an analysis that utilizes numerical adjustments to the sales prices of comparable properties relative to the subject property.

A **qualitative analysis** is an analysis that describes adjustments and the direction of adjustments; however, it does not provide numerical adjustment for various features. This is often used to describe the reasonableness of the adjustments, and may be used in conjunction with a quantitative analysis.

Sources of Comparable Data and Data Verification

Louisiana is a disclosure state, thus, documents recorded in the various parishes are available for viewing to the general public, including both sales and mortgage documents.

Many parishes now offer on-line access to the actual recorded documents. Additionally, there are other services available that provide a summary of the recorded information. Pertinent data includes vendor (seller), vendee (buyer), sales price, legal description, date of sale and recordation information. The size of the improvements, age of the improvements and municipal addresses are not typically included in the recorded document.

Note that the sales price is not legally required to reflect market value. It is simply the price noted in the legal document, and may not reflect the entire consideration paid for the real estate, or may reflect an amount above that paid for the real estate. The sales price should be verified with the seller, buyer or agents involved in the transaction, particularly when the amount is inconsistent with other market data.

There are currently thirteen local Member Boards in the State of Louisiana covering 45 parishes throughout the state that are part of the Louisiana REALTORS Association, including:

- Acadiana
- Baton Rouge
- Bayou - Houma
- Central Louisiana
- Greater Fort Polk
- Livingston
- Natchitoches
- New Orleans Metropolitan
- Northeast
- Northshore
- Northwest
- Saints
- Southwest

<http://www.larealtors.org/local/default.asp>



Verification of the size of the improvements can be obtained from the seller, buyer, real estate agent, or other knowledgeable party; however, actual measurement is the best source. Permit information is a source; however, it must be verified.

Data in multi-listing services is a good source to obtain physical property information and details on listings and sales. Consistency in measurement and in reporting is the key to quality control of data. Contacting the agent and verifying the source of the square footage, and obtaining details on the physical condition and financing arrangement, increases the usefulness of a sale as a comparable. Other important details to consider include the list price relative to the sale price, and the length of time on the market (DOM).

If a Realtor does not report concessions, use of the data is flawed without additional verification beyond the MLS service.

In analyzing data, a Realtor/appraiser should perform a more in depth search when noting a sales price greater than the list price. This could imply atypical financing, concessions, or other arrangements in which the sales price may not reflect simply the value of the property.

Areas of Comparability and Test of Comparability

In appraisal theory, the “Areas of Comparability” are also called the “Elements of Comparison”. In this analysis, the Realtor/appraiser develops the degree of similarity or differences of the comparable property relative to the subject property utilizing quantitative and/or qualitative methods.

General categories include:

1. Property Rights
2. Financing Terms
3. Conditions of Sale
4. Concessions
5. Market Condition/Date of Sale
6. Locational and Physical Features

Categories 1-4 are transactional adjustments; applied typically in the order presented. Property specific adjustments address all of the variances in location, physical, and economic features between the comparables and the subject property.

Property Rights

An adjustment for comparable property rights relative to the subject. Property rights include property interests (fee simple, leased fee, leasehold), and may reflect partial interest.

An example of a property interest adjustment is if Comparable 1 was subject to a below market lease rate. Comparable 2 is very similar, but was leasing at market. If the subject property interest is fee simple interest, or available to lease at market, the Property Rights adjustment is:

$$\begin{array}{r} \text{Sales Price of Comparable 2} \\ - \text{Sales Price of Comparable 1} \\ \hline \text{Property Rights Adjustment to Comparable 1 (+} \\ \text{relative to subject)} \end{array}$$

Financing

One must understand that a closed sale with a recorded sales price is “potentially” a comparable sale, contingent upon verification of comparability, including verification of sales price paid for the real estate.

It is not a legal requirement that the recorded sales price represent the price paid for the real estate, or the market value of the real estate. There are many recorded transactions that indicate consideration (price) of \$1.00. Verification of the actual price paid for the real estate is a necessity.

A review of the financing terms is necessary to determine if the sales price reflects “typical” financing terms. In other words, verification that the sales price was not changed from the price of the real estate to a price reflective of the real estate and special financing. If special incentives or financing was involved, this must be netted out of the sales price to determine the price paid for the real estate.

Fannie Mae and Freddie Mac compliant appraisals must indicate the type of financing for each comparable sale. The choices include:

- FHA
- VA
- Conventional
- Seller
- Cash
- USDA – Rural Housing
- Other – must be detailed

This involves adjustment of comparables for differences in motivation of either the buyer or the seller in a transaction; for example: a non-arm's length sale. Part of the data verification involves verifying the type of transaction. Appraisers, when completing a Fannie Mae or Freddie Mac compliant appraisal, are required to indicate the sale type for each comparable property. The sale type categories include:

- REO sale – real estate owned
- Short sale
- Court ordered sale
- Estate sale
- Relocation sale
- Non-arm's length sale – related parties
- Arm's length sale - unrelated parties acting in his/her own best interest
- Listing

Proper indication of the “sale type” is necessary in order to determine if the price paid reflects market value, or another value caused by a distress sale situation. A distress sale is a sale involving a seller acting under undue duress.

Remember, financial institutions require that an appraisal for mortgage purposes reflects “market value” as defined by the interagency guidelines. This requires a willing and knowledgeable buyer and seller agreeing upon a price, without undue stimulus. If a sales price is not the equivalent of the market value, the comparable must be adjusted to reflect the market value in order to relate it to the subject property.

A vendor /vendee with the same last name should always involve additional research to verify the relationship between the parties to determine if the recorded price reflects market value. A sale between related parties is considered a “Non-arm's length sale”.

A listing provides information, and comparable listings should always be considered; however, a listing is not a closed recorded sale and should not be considered as such. All else being equal, a listing would reflect the top potential price for the subject property.

Concessions

The Appraisal Institute defines a *Concession* as:

“A financial payment, special benefit, or non-realty item included in the sale contract or rental agreement as an incentive to the sale or lease. Concessions occur when the seller or lessor agrees to pay an inducement or to give some special credit or property to a buyer or lessee, who agrees to pay a higher price than the seller or lessor would normally pay in return for the inducement or credit. Concessions usually result in artificially inflated sale prices or lease rates. Often concessions allow financing that would otherwise not be possible. Concessions may be disclosed as part of the sale or lease, but often they are not.”

Federal law and national banking regulations have always required mortgages be based on market value. The definition is intended to ensure that appraisals reflect an opinion of the value of real estate, net of any special or creative financing or sales concessions.

Examples of concessions include seller's payment to buyer to repair items outside of the sales agreement; seller incentives such as cash rebate, interest buy downs, etc. Residential appraisal forms require the appraiser to certify the standardized market value definition was used, and if it isn't, not only can appraisers get into trouble with regulators, but a mortgage originator can be forced to re-purchase the loan and the note can also be called due immediately, which can cause a borrower to go into foreclosure.

The reason deduction of concessions is required is that mortgage loans are to be based only on value of real estate. Misleading a lender or lender's agent (appraiser) so that real estate is overvalued is considered mortgage fraud by the FBI. Hiding seller paid concessions from market participants can be considered "misrepresentation by omission of a material fact".

Market Condition/Date of Sale

Market condition adjustment is sometimes called the "time adjustment". It is an adjustment applied to a comparable sale to bring the sale "current", or into the same market conditions as the effective date of valuation or pricing of the subject property.

For example, if the market has improved 5% from the date of the sale to the date of analysis, and this is evidenced by market activity (i.e. sale – resale activity), then a +5% adjustment would be applied to the comparable sale.

The goal is to utilize comparable sales that are considered "current", thus, no market condition adjustment would be required. In residential valuations, Fannie Mae recommends that an appraiser utilize a sale that occurred within 12 months; however, comments are required when utilizing any sale greater than six months.

A "time" or market condition adjustment must be based on market data for the particular neighborhood and for competing locations, not on a pre-determined or assumed dollar adjustment.

Locational and Physical Features

Locational and physical features are adjusted once the sale is considered to reflect a price in the current market. In the *Identification of the Subject* section, there were a variety of categories discussed. These categories include:

- Location characteristics
- Site specific characteristics
- Use
- Improvement details

Not only is identification of the subject features necessary, it is also necessary for each comparable. Should a comparable differ from the subject in a specific category, an adjustment may be necessary. The necessity of an adjustment is based upon analysis of the market, and extraction of an adjustment from market activity. Costs are not typically equivalent to value.

Value/Price Conclusion – Test of Comparability (net and gross adjustments)

After adjustment of each comparable for variances relative to the subject, the standard deviation, or range of adjusted values should be much narrower from that indicated by the sales price range prior to adjustment.

This should occur in both in gross numbers and on a unit value basis.

There are three quantitative measures often utilized to review the comparability of the sales relative to the subject:

- line item adjustment
- net adjustment
- gross adjustment

Value/Price Conclusion – Line Item Adjustment

A **line item adjustment** is the degree of adjustment of the comparable for a single element of comparison or category. This is related as a percentage adjustment.

Value/Price Conclusion – Net Adjustment

The **net adjustment** is calculated by summing the individual positive and negative adjustments to derive the net impact of adjustments. The percentage is computed by dividing the summation by the price prior to adjustment.

Gross Adjustment

The **gross adjustment** is a summation of all adjustments, ignoring the direction of the adjustment. The percentage is computed by dividing the summation by the price prior to adjustment.

For example:

Sales Price of Comparable	\$ 700,000	Line Item Percentage
Site Adjustment	– \$170,000	– 24.29%
Quality of Construction	+ \$170,000	+ 24.29%
Living Area Adjustment	+ 15,000	+ 2.14%
Porch Adjustment	– \$5,000	– 0.71%
Net Adjustment	+ \$10,000	+ 1.43%
Gross Adjustment	\$360,000	51.43%
Adjusted Sales Price of Comparable	\$ 710,000	

Usually, the magnitude of net adjustments is a less reliable indicator of accuracy. It may be misleading because a significant amount of adjustments may be applied to relate a comparable to the subject; however, the net impact indicates little adjustment. The gross adjustment, however, would measure all of the adjustments, and may indicate a limited degree of reliability of a comparable.

A review of the net adjustment in the previously presented example indicates strong comparability, with a net adjustment of only 1.43% from the sales price to the adjusted value. The gross adjustment, however, indicates the significant degree of adjustment applied to the comparable relative to the subject. The comparable was adjusted over 50% for varying elements relative to the subject.

There are guidelines for measuring comparability; however, these are not rules. Limited sales data, or unique quality, condition, location, etc., may result in large adjustments to even the best chosen comparable sales.

Typically, users of appraisal reports request discussion of any adjustments that far exceed desired parameters - in other words, a qualitative analysis beyond the quantitative analysis. The following parameters are often used by underwriters when reviewing appraisal reports, particularly single family residential reports (these are not requirements by Fannie Mae or Freddie Mac:

Adjustment Category	Recommended User Range
Line Item Adjustment	<10%
Net Adjustment	<15%
Gross Adjustment	<25%

In appraisal theory, the conclusion of a value is called “reconciliation”. This is not synonymous with averaging the adjusted sales prices to determine value. The process involves weighting the comparability of each sale, reviewing all of the data gathered in the valuation process, including listing data, market condition data, property specific data, etc., and forming an educated opinion of value. In a contract sales scenario, it is reasonable for an appraiser to conclude at contract price, if such a conclusion is within the range of reasonableness and the appraiser's opinion is that such a price is consistent with the definition of market value.

Broker Price Opinion

In this section we will look at all aspects of the Broker Price Opinion, all a part of qualifying the property. It basically answers two questions. 1: What is the property value? And for the broker's purpose, “What can it sell for?” Very often these two things are hardly the same.

Property Pricing

The real estate industry draws from a number of disciplines, including architecture, law, engineering, finance, construction, etc.

The primary real estate activity, and probably the best known, is real estate brokerage, in which individuals act as agents to bring property sellers and buyers together to consummate transfers of real estate.

A real estate transaction is a complicated process in which numerous professionals become involved to coordinate the activities necessary to complete the sale.

A successful real estate brokerage operation is dependent upon a number of factors, probably the most important is an inventory of listings of properties for sale. Advertising listings draws property seekers to the brokerage operation, from which transactions can emanate.

While listings are the life blood of a brokerage operation, it is obviously important for the broker to price properties realistically. Typically, the listing price is established by negotiation between the broker and the property owner. Obviously, the property owner wants to achieve the highest possible price. However, the broker needs to accept only listings at prices which are likely to generate interest.

A tool which has been used for years to assist the broker is estimating a probable sales price is the broker price opinion (BPO), which is alternatively referred to as a competitive market analysis (CMA).

Real estate appraisal is defined as “the act or process of establishing value.” Clearly, the appraisal function is concerned with valuation. Appraisers employ theory and methodology for the express purpose of generating an estimate of property value.

Real estate brokers utilize some of the same methodology in developing a broker price opinions (BPO) or a competitive market analysis (CMA). Historically, appraisals have been more sophisticated than price opinions, primarily because the appraisal report has been required to meet standards which are inherent in a price opinion.

Over the years, real estate appraisals have become more complex documents subject to increasing requirements. Originally, an appraisal might have consisted of a two-page form with a photograph attached.

Most real estate appraisals are made in conjunction with the loan underwriting process. Financial institutions have developed underwriting policies regarding appraisal content.

Since many residential real estate loans are sold in the secondary market, there are guidelines which have been instituted by secondary market participants, most notably FNMA (Fannie Mae). These policies and guidelines have served to make appraisal reports more uniform. The amount of documentation in an appraisal report has increased significantly over the years.

What follows is a discussion of the general concept of price opinions.

The objective of this presentation is to provide information about appraisal theory and methodology to enable understanding of the process of property pricing.

According to the Uniform Standards of Professional Appraisal Practice (USPAP), there are two levels of valuation activity.

They are **Valuation Services**, defined as “services pertaining to aspects of property value”, and **Appraisal Practice**, which is defined as “valuation services performed by an individual acting as an appraiser”. Valuation services can be performed by anyone, but appraisal practice is a valuation service provided by an individual acting as an appraiser, subject to rules and regulations regarding appraisals.

An appraisal by definition carries a level of expertise and sophistication, as well as an expectation that the result will be supported by market data. An appraisal is expected to be performed in an independent, objective and impartial manner.

A **Broker's Opinion of Value (BOV)** is defined as “An opinion of value developed by a real estate agent or broker rather than by a licensed or certified appraiser.” (The Dictionary of Real Estate Appraisal, AI, 5th Edition)

A **Broker's Price Opinion (BPO)** is defined as “An opinion of property price rendered by a licensed real estate agent or broker.” (The Dictionary of Real Estate Appraisal, AI, 5th Edition)

A **Competitive Market Analysis (CMA)**, which is “a listing tool that a sales agent prepares in order to show a seller what the home is likely to sell for, and the CMA helps the agent decide whether or not to accept the listing.” (Real Estate Principles, 8th Edition, Charles J. Jacobus)

A **Comparative Market Analysis (CMA)** is defined as “A method of determining the value of real property used by appraisers and real estate brokers that compares actual recent sales of similar local properties to arrive at an indicated value. Small differences in the properties are assigned positive or negative dollar values to allow for direct comparison.” (Dictionary of Real Estate, Prentice Hall)

These definitions all relate to efforts by sales agents to establish a probable price for the express purpose of listing properties for sale

From Louisiana Appraiser Law, Broker Price Opinion/Comparative Market Analysis “...an analysis of recent sales of similar properties by a real estate salesperson or broker to derive an indication of the probable sales price of a particular property for the salesperson's or broker's principal.”

Per Appraiser Law “nothing shall preclude a licensed real estate broker or salesperson from performing a broker price opinion/comparative market analysis in the ordinary course of the practice of real estate, provided that the broker or salesperson does not represent himself as being a state licensed real estate appraiser.”

The suggestion here is that while the price opinion is considered to be for the purpose of establishing list price for brokerage purposes, the law does not preclude a sale agent from performing a price opinion for any purpose, as long as the agent does not hold himself out as an appraiser.

The price opinion was developed as a tool for use by a broker in the listing process. The level of sophistication was historically minimal.

A price opinion might be developed by an agent collecting property sales in the area and dividing the respective sales prices by the square footage of living area to develop a range of unit prices.

Like appraisals, price opinions have increased in sophistication. Enhanced technological capabilities have been instrumental in developing price opinion products.

In the recent past, price opinions have evolved from being a tool utilized by brokerage people for listing purposes to being a substitute for an appraisal in lending situations. Financial institutions engage in transactions with different levels of risk. It has become a popular practice for financial institutions to utilize alternatives to appraisals in what they consider to be low risk situations in order to reduce fees.

Appraisal practice is regulated by the Uniform Standards of Professional Appraisal Practice (USPAP). USPAP establishes specific requirements for appraisals. Since price opinions do not meet USPAP requirements, they are typically not performed by appraisers. Therefore, they do not typically carry the level of expertise typically found in an appraisal.

According to Louisiana appraiser law, a sales agent can perform a price opinion for any purpose, as long as they do not refer to themselves as an appraiser.

The price opinion has become a tool which has multiple uses, and upon which more people have come to depend. There are trade organizations which have emerged for the express purpose of training and offering business opportunities to individuals interested in performing price opinions.

For example, there is:

NABPOP, which is the National Association of Broker Price Opinion Professionals, which advertises BPO education and training, BPO certification authority, BPO standards and guidelines and BPO political activity.

“a BPO is an excellent means of information for banks and lenders to make financial decisions on residential properties. Due to the financial practicality and quick turnaround time of a BPO, banks and lenders order BPOs from a BPO Company.

BPOs have become a lucrative niche in the real estate industry for Real Estate Professionals. Performing BPOs have become a reliable source of either supplemental income or the sole source of income for many real estate professionals across the country.

A BPO Company acts as a clearing house for banks and lending institutions by contacting real estate professionals and assigning BPO jobs to them, tracking and expediting BPO job status, and providing quality assurance/oversight for submitted BPOs from the real estate professionals. “

The NABPOP organization is cited herein as an example. No effort is made to endorse the activities of the organization. It appears to be one of several website based organizations dedicated to promotion of BPO use.

The National Association of Realtors has adopted a “Responsible Valuation Policy.” Standard of Practice 11-1 states that “when REALTORS® prepare opinions of real property value or price, other than in pursuit of a listing or to assist a potential purchaser in formulating a purchase offer, such opinions shall include the following unless the party requesting the opinion requires a specific type of report or different data set:

1. identification of the subject property
2. date prepared
3. defined value or price
4. limiting conditions, including statements of purpose(s) and intended user(s)
5. any present or contemplated interest, including the possibility of representing the seller/landlord or buyers/sellers
6. basis for opinion, including applicable market data
7. if the opinion is not an appraisal, a statement to that effect”

The Responsible Valuation Policy includes the following:

Appraisals

- Persons who perform appraisals of real property shall be licensed or certified by their respective state regulatory agency and the appraisal shall conform to standards established in the Uniform Standards of Professional Practice (USPAP).
- No person with an interest in the mortgage transaction shall compensate, coerce, extort, collude, instruct, induce, bribe, or intimidate a person, appraisal management company, or firm for the purpose of influencing the appraised value to be unfairly and improperly adjusted.

Non-Appraisal Opinions

- Non-appraisal opinions, such as Broker Price Opinions (BPO) and comparative market analyses performed by REALTORS shall contain, at a minimum, the information specified in Standard of Practice 11-1 of the National Association of REALTORS® Code of Ethics except where the party requesting the opinion requests a specific type of report or different data set, or where the opinion is developed in pursuit of a listing or to assist a potential purchaser in formulating a purchase offer.

Among other uses, these non-appraisal services can help determine listing prices and are used to estimate potential selling prices of a property. Except where exempted or prohibited by the National Association of REALTORS® Code of Ethics, state, local or federal law, they should include the disclosure of a review of the subject property, subject neighborhood review and analysis, local and regional market information and trends, and a description of comparable properties that are similar to the subject property. Any non-appraisal opinion that does not provide the aforementioned components shall be disclosed by the provider of the service. Non-appraisal opinions must make it clear to the intended user that it is not an appraisal.

- Non-appraisal opinions shall be prepared by a real estate licensee or registered, licensed or certified appraiser. A licensee completing these services for a client is not necessarily assured of receiving the listing of the property.
- Generally, in conjunction with the purchase of a consumer's principal dwelling, BOPs may not be used as the primary basis to determine the value of real property for the purpose of a loan origination of a residential mortgage loan secured by such property.
- When not restricted by law, non-appraisal opinions may be appropriate for many real estate transactions such as short sales, foreclosures, and loan modifications.
- In adhering to Article 11 of the REALTORS® Code of Ethics, consideration must be given to the intended use and intended user when developing any valuation.
- A comparative market analysis (CMA) is generally used to provide information to sellers or buyers in determining listing price or offering price."

As can be seen, the fundamental purpose behind the traditional price opinion has expanded from being a tool utilized for listing purposes to an acceptable valuation premise. Price opinions have gained wide acceptance within the lending community

The key to any valuation effort is the quality of the analysis, which is a function of the data available and the skill of the individual performing the analysis. This relates to appraisal methodology, in that appraisers understand that the credibility of any comparative analysis is the quality of the sales data utilized to develop the value conclusion. This holds true for the most detailed and complete appraisal to the most minimal price opinion.

A price opinion can be a very unsophisticated model, as mentioned earlier. It can be merely a listing of sales prices reduced to some unit indicator, most probably square footage.

On the other hand, it can be a much more detailed presentation similar to an appraisal report. There are numerous proprietary products available, such as those developed by Fannie Mae, Freddie Mac and individual financial institutions. Examples of these forms are included herein. Some of these forms very closely resemble appraisal reports, and include a grid for specific adjustments. It is apparent that for the more sophisticated models, considerable training is necessary to complete.

The basic assumptions in preparation of a credible price opinion are the same as those which apply to an appraisal. First, it is presumed that the property is accurately identified and described, and that all of the relevant property characteristics are accounted for. Then, it is presumed that the preparer has access to reliable comparable data. For residential purposes, the most likely data source is MLS. In fact, some MLS providers offer a CMA product which can be automatically prepared within the program.

If these circumstances exist, the simplest price opinion model could include only an overall unit indicator, such as sales price/square foot of living area. Assume a subject property which is a 20-year old brick veneer structure in a residential subdivision comprised of similar structures, containing approximately 2,000± square feet of living area, three bedrooms-two bathrooms, and a double carport.

Property	Sale Price	Living Area SF	SP/SF
SALE #1	\$165,000	1,860 SF	\$ 88.71
SALE #2	\$178,000	1,980 SF	\$ 88.90
SALE #3	\$172,000	1,900 SF	\$ 90.52
SALE #4	\$160,000	1,800 SF	\$ 88.90
SALE #5	\$185,000	2,120 SF	\$ 87.26

Assuming all of the sales are relatively recent and similar in location, it appears that there is uniformity in the price level. The indicated unit value for subject would be about \$89 to \$91 per square foot of living area. This appears to be unusually narrow range of prices and unit indicators, however.

Alternatively, the property could be analyzed using the same sales data and a form, such as the FNMA product, with each sale adjusted for differences between it and subject.

Appraisers typically make adjustments for one or more elements of comparison, which include

Transactional Adjustments:

- 1) real property rights conveyed
- 2) financing terms
- 3) conditions of sale
- 4) expenditures made immediately after purchase
- 5) market conditions .

Property Adjustments:

- 1) location
- 2) physical characteristics
- 3) economic characteristics
- 4) use/zoning
- 5) non-realty components of value

For residential properties, the adjustments which typically are made are for 1) rights conveyed (typically fee simple), 2) financing (concessions), 3) location, and 4) physical characteristics (lot size, design/appeal, quality, age/condition, room count, living area square footage, HVAC, automobile storage, etc.). Obviously, the more comparable the property, particularly in location, the less complicated the adjustment process.

There are general rules which tend to apply for making adjustments. For example, all other things equal, older properties tend to sell for less than newer ones.

All other things equal, larger properties will sell for more than smaller ones, but the unit price (sale price per square foot) will decline as the residence size increases.

When a property sale includes the seller paying costs typically borne by the buyer (closing costs, for example), a negative adjustment to that sale is required. Also, the traditional treatment of adjustments is that if the subject is superior to the comparable, a positive adjustment is indicated. Conversely, if subject is inferior to the comparable, the adjustment is negative.

While most real estate practitioners are familiar with these tendencies, the specific magnitude of the adjustment necessary to equate a comparable with a subject is not so easy. For example, in the previous example, Sale# 4 has 200 square feet less than the subject. If an adjustment for difference in square footage is required (such as on the FNMA BPO form), then it is clear that a positive adjustment needs to be applied to Sale # 4. While the direction of the adjustment is relatively simple, the magnitude of that adjustment is somewhat complicated.

Another method of valuation is the Cost Approach.

Conceptually the cost approach means a potential real estate buyer should not pay more for a property than it would cost to build its equivalent.

The cost approach method is an estimate of the replacement value of a property determined by the cost of the land and improvements, then subtracting its depreciation.

The steps of the cost approach are:

1. Estimate the value of the land as if vacant.
2. Estimate the building's replacement cost.
3. Estimate the building's loss by depreciation.
4. Subtract the depreciation from the estimated replacement cost.
5. Calculate the value of the property by adding the estimated land value to the depreciated value of the building.

The most difficult part of the cost approach is accurately estimating depreciation.

You have to consider every aspect of depreciation –

Physical, which is wear, tear and deterioration.

Functional – the look, feel, form and style of the property

And locational factors – what things outside the property will influence the value.

So let's look at an example of the cost approach calculations.

The first step is to: estimate the value of the land as if vacant.

Equitable property in the surrounding area is going for \$2,000 an acre.

The residence sits on an acre and a half.

The estimated land value would be \$3,000

The next step is to estimate the building's replacement cost.

3,000' sq @ \$80 per	\$240,000
Other improvements	15,000
<u>Driveway and landscaping</u>	<u>18,000</u>
Estimated cost – new	\$283,000

The third step is to estimate the building's loss by depreciation.

Depreciation calculations can be very subjective and based on the experience of the agent/broker, the location and overall structure factors involved. Ten agents could come up with ten very different price opinions.

For our estimate we are going to keep it simple and factor in depreciation cost of major components and then look at the age factor against the replacement cost to come up with a total depreciated value.

There does not appear to be any functional or external obsolescence for our example, but if there were you would simply add those into the overall depreciation.

Physical: Roof, HVAC, Flooring, Misc.

Cost: \$42,000 x 33% depreciation = \$13,860

Age of structure = 20 years

\$283,000 x 33% = \$ 93,390

Total Depreciation = \$ 107,250

Next, subtract the total depreciation from the estimated replacement cost.

Replacement Cost	=	\$ 283,000
<u>— Total Depreciation</u>	=	<u>\$ 107,250</u>
Depreciated value	=	\$ 175,750

Finally, calculate the value of the property by adding the estimated land value to the depreciated value of the building.

Depreciated value	=	\$ 175,750
<u>+ Land value (step 1)</u>	=	<u>\$ 3,000</u>
Cost approach value	=	\$ 178,750

The cost approach is more reliable when improvements are new or near-new. For older structures, this approach may not be the best choice because of the greater subjectivity involved in estimating accrued depreciation.

In this case the buyer should not pay more than \$178,750 for the comparable home.

Another method of property valuation is the **Income Approach**.

The **Income Approach** allows investors to estimate the value of a property based on the income it will produce:

The income approach is used primarily for income producing properties such as apartment complexes and office buildings. It anticipates a flow of income based on two things.

- 1: Market rent – what the property earns (This is the rental income)
- 2: Resale Value – When the property is sold

A key component to the income approach is the **Capitalization Rate**, or the rate of return the investor wants to earn from the property.

The formula to determine the Cap rate is:

$$\text{Capitalization Rate} = \frac{\text{Net Operating Income}}{\text{Current Market Value}}$$

So if the investor wants to earn 10% we can factor that in and now with this calculation...

$$\text{Current Market Value} = \frac{\text{Net Operating Income}}{10\%}$$

Once we calculate the Net Operating income we will have the Market Value of the property.

Net Operating Income is cash remaining after deduction of operating expenses and rental collection losses.

Potential Gross Income

28 Units @ \$1,100 per month = \$ 30,800

— 6% Vacancy/Collection loss = \$ 1,848

Effective Gross Income (EGI) = \$ 28,952

Annualized EGI (x12) = \$347,424

Now that you have your Estimated annual income you would have to subtract the operating expenses. These would be for maintenance and upkeep expenses, salaries, property taxes, common utilities, insurance and any other cost to the operation.

For this example, those totaled to be \$122,587 annually roughly 35% of the income, giving us a total net operating income of \$ 224,837.

Current Market Value is the Net Operating Income divided by the market capitalization rate desired by the investor.

$$\text{Current Market Value} = \frac{\$224,837}{10\%}$$

\$ 2,248,370

The income approach only looks at the rent potential for the property. It may not take into account other features such as the property's condition or the value impacts of the neighborhood.

The income approach gives a quick snapshot of what a particular piece of rental property might be worth.

A **Gross Income Multiplier (GIM)** is simply a ratio of property value to gross income and can be used to evaluate whether the price of a specific income property is a good deal.

The formula to determine the GIM is:

$$\text{GIM} = \frac{\text{Sale Price}}{\text{Effective Gross Income}}$$

To calculate the GIM as it relates to a property the investor is looking to purchase, select a number of other properties similar in terms of size, price, location, rents and expense, to compare to the investor's subject property.

For example, the investor is looking at a piece of property with an Effective Gross Income of \$78,000. The Sales price on the property is \$546,000 so we can calculate the GIM to be 7.

$$\text{GIM} = \frac{\$ 546,000}{\$ 78,000} = 7$$

Let's look at a collection of properties the agent chose to compare to the investors property.

Address	Sales Price	EGI	GIM
127 Oak St	\$ 592,000	\$ 84,000	7.1
17 Ash Way	\$ 527,000	\$ 63,000	8.3
1610 Poplar	\$ 541,000	\$ 84,000	6.4
26 Utopia Dr	\$ 510,000	\$ 76,000	6.7

We already know the investors property has a GIM of 7. Looking at the comparables we can see that 7 GIM falls within the range of these comparable properties.

Now that you have compared the subject property to a few comparables, you should then take the average of your compares. Doing this will equalize the data, in case one or more of the properties has an unusually high or low GIM.

To calculate this average, add the GIM figures of each property and divide by the number of comparables, in our case 4.

The average of our four comparables is 7.1 – in-line with the investors subject property.

The GIM method is good for a quick comparable estimate but a more comprehensive appraisal should be made prior to the transaction of sale.

The Gross Rent Multiplier (GRM) is the ratio of the price of a real estate investment to its monthly rental income before expenses.

You could also think of it in terms of the number of months the property would take to pay for itself in gross received rent.

The Gross Rent Multiplier (GRM) approach is normally used in valuing single-family homes and small residential income properties such as duplexes, threeplexes or fourplexes.

Instead of annual income, the GRM Approach considers the relationship between gross monthly rents and price. It, too, is a method more akin to a comparative sales approach for the same reasons stated above.

The formula for the GSM is:

$$\text{GRM} = \frac{\text{Sales Price}}{\text{Scheduled Gross Rent}}$$

For example: Consider a single family property to be used as rental income. The house is for sale for \$100,000. The rent is expected to be \$1,000 per month.

$$8.33 = \frac{\$ 100,000}{\$ 12,000}$$

When you annualize the rent you come up with \$12,000 as the scheduled gross rent income. Divide that by the sale price and you come up with a GRM of 8.33.

Now let's compare that to some equitable rental properties in the vicinity.

Address	Sales Price	Rent Inc	GRM	Monthly Rent
45 North Lane	\$ 100,000	\$ 11,400	8.78	\$ 950
126 Sparrow Dr.	\$ 120,000	\$ 12,600	9.52	\$ 1,050
411 Concorde Pl.	\$ 123,000	\$ 13,200	9.31	\$ 1,100
263 River Rd.	\$ 95,000	\$ 10,440	9.10	\$ 870

All of the comparables return a higher GRM.

A lower GRM multiplier means you are getting more rent for each dollar of value and provides a higher rate of return.

The GRM method should be a "rule of thumb" quick look at rental properties only. It does not consider the full reality of an investment. For example, you only calculate the full scheduled rent income which may not occur due to vacancies.

In better neighborhoods properties be rented longer with less turnover than other rent challenged neighborhoods. Cost of ownership can be much higher when tenants frequently change.

The GSM should let you know whether this may or may not be a good investment. A more comprehensive appraisal should be secured prior to making an offer on the property.

Valuation by Certified Appraiser

In this section we'll take a quick look at some of the general requirements for appraisers.

An appraisal by a licensed real estate appraiser must be completed in order to determine if a property is eligible for a Federal Housing Administration loan.

Most mortgage lenders will demand an appraisal by a licensed real estate appraiser prior to loan closing and in most cases the appraisal is a contingency of final loan approval.

Appraisal by a licensed real estate appraiser must follow standards set by the Uniform Standards of Professional Appraisal Practice (USPAP), to meet Federal appraisal guidelines.

While USPAP provides a minimum set of standards for appraisals in the U.S., it does not prescribe specific methods the appraisers should use.

USPAP only requires appraisers be familiar with and correctly use methods which would be acceptable to other appraisers and acceptable to the intended users of the appraisal.

Appraisers are obligated to gather specified preliminary data about the property, such as the type property being appraised, the basis of value (e.g. market, investment, impaired, unimpaired), the interests appraised (e.g. fee, partial), important assumptions or hypothetical conditions, and the effective date of the valuation.

Based on this and other key information, the appraiser arrives at an informed estimation of property value.

Appraisal price opinion is based purely on current property circumstances and market value only. The appraisal should never try to estimate future value.

The licensee offering the price opinion should remain objective and stick exclusively to the facts of the current market value without offering undue pressure to the buyer or seller.

Property Pricing Case Study – REDBUD

In this section we are going to step through a case study to look at how an agent would look at comparables in a neighborhood to develop a valuation on a specific piece of property.

We'll look through the history of the location to see how any external circumstances might influence value. We'll get very specific about each comparable so a thorough evaluation can be made.

Our case study is a place called **Redbud**.

Redbud is a bedroom community with a population of approximately 20,000± persons, located about 20 miles from a metropolitan area, Unrealville.

Highway 12, known as the Redbud Road, is a newly four-laned thoroughfare which connects Redbud, as well as other similar communities located west of Redbud to Unrealville.

Unrealville is a growing center of commerce and industry. Governmental offices, financial institutions, retail and office commercial operations are located there. The population has grown steadily over the past few years. All economic indicators, including population, employment and income, are positive.

There has been a national recession which has affected economic conditions over the past few years, however, the Unrealville metropolitan area has experienced less negative effect than other cities regionally and nationally.

Redbud is located relatively near to Unrealville, with convenient access. It has benefitted over the years from its proximity to the city, from an employment perspective, as many of its residents commute into the city for work, but also because of its medical facilities, and cultural and entertainment venues. Redbud is a quiet, peaceful community, often described by its residents as "a wonderful place to live and raise a family."

The market area is considered to be reasonably stable. According to a state agency, the population of the entire metropolitan area has increased approximately eight percent over the past decade. Property values in general have increased.

A local appraiser has recently done a study and determined that the typical price change, demonstrated by a paired sales analysis, for residences in Redbud, has been an increase of approximately six percent per year for the past 2-3 years.

Approximately 30 years ago, a successful developer/homebuilder named Jones, acquired a parcel of land on Highway 12 in Redbud for the express purpose of developing a residential subdivision. He subdivided the tract into a development he named Redbud Heights, with 100 residential lots typically measuring about 80 feet by 150 feet.

The terrain is flat and level, and there are no unusual physical features. All of the lots have essentially the same view and topography.

The development is zoned for detached single family residential use, and there are recorded subdivision restrictions which establish building requirements. The development was considered to be well located with respect to local amenities, and additionally was located just off of the major access route to Unrealville.

Based on the locational and physical characteristics of the property, there was good demand for homes in the development. Within three years, Jones had constructed and sold 92 of the 100 lots with traditional residential structures ranging in size from approximately 2,000 to 2,400 square feet (living area).

The level of quality was average, and floor plans were functional. Design and appeal of the residential properties was considered to be good, and the development had immediate success.

Several years ago, Highway 12 was widened to facilitate the increasingly heavy traffic flow between outlying communities, including Redbud, and Unrealville. The traffic flow on Highway 12 is heavy at times. The combination of increased traffic volume and noise from that traffic has made Redbud Heights somewhat less desirable, particularly when compared to newer subdivisions located off of the main thoroughfare.

A trend which has developed over the past decade is toward a higher number of rental properties in Redbud, including the subject subdivision. Reportedly, about 20 percent of homes in Redbud Heights are tenant occupied. Rental levels are typically between \$1,400 and \$1,600 per month. The demand for rental properties in Redbud is attributed to a number of factors, particularly transient job opportunities in and around Unrealville.

There are no vacant sites in the subject subdivision at present, nor have there been any recent land sales. Sales of vacant lots in other similar developments indicates that the typical lot in the subject subdivision is approximately \$30,000.

Jones retained eight of the original 100 lots for future sale or construction. His health deteriorated and the lots remained in his inventory for about 20 years, until his death approximately 12 years ago.

At that time, another developer, Thomas, acquired the remaining eight lots out of the estate of Jones. Thomas felt he got a really good deal, and that he had been able to acquire the lots at a substantial discount from market. He built houses on four lots, and they were sold immediately.

Thomas had two friends, the Smith brothers. The Smith brothers approached Thomas about four contiguous lots located at the front of the development. They wanted to build adjoining personal residences and wanted larger building sites than the typical single lots.

The brothers acquired the four lots at what they felt were bargain prices, and each constructed a residence. The respective residential structures were built utilizing both lots. Re-subdivision of lots was prohibited by zoning, but the residences were constructed across the lot line, effectively creating two lots twice the size as the typical site.

The Smith brothers built homes which were intended to "last a lifetime". The residences were superior in quality to the typical property, with amenities including high ceilings, extensive crown molding, etc. Appliances, plumbing and mechanical equipment, and HVAC were all more modern and higher quality.

The Smith residences were about the same size as the larger residences in Redbud Heights (approximately 2,200± square feet) but were newer than the original structures. It was reported that the Smith residences cost about 30 percent more to build than the other houses which were built at about the same time.

The Smith brothers felt that the additional cost was justified because the lots were obtained at a favorable price, and because they both intended to live in the respective residences as long as they lived.

About two years ago, Smith brother #1 became ill. He died shortly thereafter. His residence was placed on the market for sale. After about a year, the property went under contract.

The pending sale was dependent upon a conventional mortgage loan (80% LTV, 5% interest, 20-year amortization), however the sale fell through because the appraisal prepared for the bank was lower than the sale price. The seller was offended and refused to negotiate the price. In order to preserve the transaction, the seller offered to owner finance with the same terms, except that the interest rate was reduced to 3 percent. The seller justified the interest rate because the rate which could have been obtained on a certificate of deposit was only 1 percent, so it was a "win-win".

The Smith #1 property sold one year ago for \$318,750, subject to the terms described. Specifically, the residence had 2,200± square feet of living area, with four bedrooms and 2.5 bathrooms. As noted, its quality level was superior to the typical residence. It was newer than the original structures, and it had been very well maintained. The residence also had an oversized garage, porches and a patio. The lot was larger than typical, and it had superior site improvements (driveway, fencing and landscaping).

There have been five other sales of residences in Redbud Heights in the past year. They are summarized as follows:

Sale 1 – this is one of the original houses built by Jones. It is a 30-year old structure of standard design/appeal, with quality similar to others in the development. It has an 80 foot by 150 foot lot with typical characteristics. The lot is located near the rear of the subdivision, and is considered to be similar to the subject location.

The residence has 2,000± square feet of living area, a double carport, storage room, porches, and site improvements (concrete driveway, landscaping, fencing). There are four bedrooms, two bathrooms, typical kitchen, fireplace, and typical HVAC, mechanical, and plumbing equipment. Interior finish has been upgraded somewhat over the years (new carpeting, wall covering, etc.). There has been no significant remodeling, but the property was very clean and well maintained.

It sold for \$212,000, with conventional financing at rates and terms readily available in the market. Date of sale was about six months ago. The property was listed on the market for approximately 60 days.

Sale 2 – this is one of the original houses built by Jones. It is a 30-year old structure of standard design/appeal, with quality similar to others in the development. It has an 80 foot by 150 foot lot with typical characteristics. The lot is located near the rear of the subdivision, and is considered to be similar to the subject location.

The residence has 2,200± square feet of living area, a double carport, storage room, porches, and site improvements (concrete driveway, landscaping, fencing). There are four bedrooms, two bathrooms, typical kitchen, fireplace, and typical HVAC, mechanical, and plumbing equipment. Interior finish has been significantly upgraded over the years. In addition to new carpeting, wall covering, etc., the kitchen and bathrooms have been modernized (new fixtures, counter tops, etc.). The property has been very well maintained, and condition is described as "like new".

It sold for \$229,000, with conventional financing at rates and terms readily available in the market. Date of sale was about three months ago. The property was listed for about 90 days prior to sale. .

Sale 3 – this is one of the original houses built by Jones. It is a 30-year old structure of standard design/appeal, with quality similar to others in the development. It has an 80 foot by 150 foot lot with typical characteristics. The lot is located near the rear of the subdivision, and is considered to be similar to the subject location.

The residence has 2,000± square feet of living area, a double carport, storage room, porches, and site improvements (concrete driveway, landscaping, fencing). There are four bedrooms, two bathrooms, typical kitchen, fireplace, and typical HVAC, mechanical, and plumbing equipment. Interior finish is essentially original. While the interior finishes have been changed and maintained, the residence is "tired". There has been no significant remodeling. The property was clean but the maintenance level is less than typical.

It sold for \$214,000, with conventional financing at rates and terms readily available in the market. Date of sale was about three months ago. The property was listed for sale for approximately 120 days. .

Sale 4 – This is one of the houses constructed by Thomas about 12 years ago. It has standard design/appeal, with quality similar to others in the development, but is newer. It has an 80 foot by 150 foot lot with typical characteristics. The lot is located near the rear of the subdivision, and is considered to be similar to the subject location.

The residence has 2,200± square feet of living area, a double garage, storage area, porches, and site improvements (concrete driveway, landscaping, fencing). There are four bedrooms, 2.5 bathrooms, typical kitchen, fireplace, and typical HVAC, mechanical, and plumbing equipment. Interior finish is original. There has been no significant remodeling, but the property was very clean and well maintained.

The property was sold about two months ago by the original owner and rented to a local bank officer. The tenant vacated the property after acquiring a house in Unrealville. Rather than rent the property again, the owner decided to sell. The property sold for \$250,000, with conventional financing at rates and terms readily available in the market. Date of sale was about two months ago. It was exposed to the market for approximately 60 days.

Sale 5 - This is one of the houses originally constructed by Jones about 30 years ago. It has standard design/appeal, with quality similar to others in the development. It has an 80 foot by 150 foot lot with typical characteristics. The lot is located near the rear of the subdivision, and is considered to be similar to the subject location.

The residence has 2,000± square feet of living area, a double garage, storage area, porches, and site improvements (concrete driveway, landscaping, fencing). There are four bedrooms, 2 bathrooms, typical kitchen, fireplace, and typical HVAC, mechanical, and plumbing equipment. Interior finish is original. There has been no significant remodeling, but the property was very clean and well maintained. The property was sold by the original owner.

It sold for \$218,000, with conventional financing at rates and terms readily available in the market. Date of sale was about two months ago. It was exposed to the market for approximately 60 days.

SALE	DATE	PRICE	SIZE-SF	ROOMS	QUALITY	AGE	OTHER
1	6 mo	\$118,200	2,000	4/2	Typical	30± yrs	Standard
2	3 mo	\$136,750	2,200	4/2	Typical	30± yrs	Standard
3	3 mo	\$104,900	2,000	4/2	Typical	30± yrs	Standard
4	2 mo	\$169,100	2,200	4/2.5	Typical	10± yrs	Standard
5	3 mo	\$126,750	2,000	4/2	Typical	30± yrs	Standard
6	12 mo	\$218,750	2,200	4/2.5	Superior	10± yrs	Owner Fin

III. COMPETITIVE CLOSED SALES									
ITEM	SUBJECT	COMPARABLE NUMBER 1			COMPARABLE NUMBER 2			COMPARABLE NUMBER 3	
Address	Redbud Heights Blvd	Another Street			Another Street			Another Street	
Proximity to Subject		REO/Corp <input type="checkbox"/>			REO/Corp <input type="checkbox"/>			REO/Corp <input type="checkbox"/>	
Sale Price	\$	\$ 212,000			\$ 229,000			\$ 214,000	
Price/Gross Living Area	\$ Sq. Ft.	\$ 106/ Sq. Ft.			\$ 104/ Sq. Ft.			\$ 107/ Sq. Ft.	
Sale Date & Days on Market		6 mos ago 60 days			3 mos ago 90 days			3 mos ago 120 days	
VALUE ADJUSTMENTS	DESCRIPTION	DESCRIPTION	+(-) Adjustment		DESCRIPTION	+(-) Adjustment		DESCRIPTION	+(-) Adjustment
Sales or Financing Concessions		Cash Conventional	0		Cash Conventional	0		Cash Conventional	0
Location (City/Rural)	City - Good	Same	0		Same	0		Same	0
Leasehold/Fee Simple	Fee	Fee	0		Fee	0		Fee	0
Lot Size	160x150	80x150	+20,000		80x150	+20,000		80x150	+20,000
View	Typical	Typical	0		Typical	0		Typical	0
Design and Appeal	Typical	Typical	0		Typical	0		Typical	0
Quality of Construction	Good	Average	+20,000		Average	+20,000		Average	+20,000
Year Built	12 yrs ago	30 yrs ago	+20,000		30 yrs ago	+20,000		30 yrs ago	+20,000
Condition	Good	Average	+12,000		Average	+ 5,000		Average	+15,000
Above Grade	Total Bdrms Baths	Total Bdrms Baths			Total Bdrms Baths			Total Bdrms Baths	
Room Count	9 4 2.5	9 4 2	+ 1,000		9 4 2	+ 1,000		9 4 2	+ 1,000
Gross Living Area	2200 Sq. Ft.	2000 Sq. Ft.	+10,000		2200 Sq. Ft.	0		2,000 Sq. Ft.	+10,000
Basement & Finished Rooms Below Grade	N/A	N/A	0		N/A	0		N/A	0
Functional Utility	Typical	Typical	0		Typical	0		Typical	0
Heating/Cooling	Central HVAC	Central HVAC	0		Central HVAC	0		Central HVAC	0
Energy Efficient Items	Typical	Typical	0		Typical	0		Typical	0
Garage/Carport	2G	2 CP	0		2 CP	0		2 CP	0
Porches, Patio, Deck Fireplace(s), etc.	Porches, FP	Porches, FP	0		Porches, FP	0		Porches, FP	0
Fence, Pool, etc.	Fence, LS	Fence, LS	0		Fence, LS	0		Fence, LS	0
Other	Typical	Typical	0		Typical	0		Typical	0
Net Adj. (total)		☒ + ☐ -	\$ 83,000		☒ + ☐ -	\$ 66,000		☐ + ☐ -	\$ 86,000
Adjusted Sales Price of Comparable			\$295,000			\$290,000			\$300,000

III. COMPETITIVE CLOSED SALES									
ITEM	SUBJECT	COMPARABLE NUMBER 1			COMPARABLE NUMBER 2			COMPARABLE NUMBER 3	
Address	Redbud Heights Blvd	Another Street			Another Street			Another Street	
Proximity to Subject		REO/Corp <input type="checkbox"/>			REO/Corp <input type="checkbox"/>			REO/Corp <input type="checkbox"/>	
Sale Price	\$	\$ 212,000			\$ 229,000			\$ 214,000	
Price/Gross Living Area	\$ Sq. Ft.	\$ 106/ Sq. Ft.			\$ 104/ Sq. Ft.			\$ 107/ Sq. Ft.	
Sale Date & Days on Market		6 mos ago 60 days			3 mos ago 90 days			3 mos ago 120 days	
VALUE ADJUSTMENTS	DESCRIPTION	DESCRIPTION	+(-) Adjustment		DESCRIPTION	+(-) Adjustment		DESCRIPTION	+(-) Adjustment
Sales or Financing Concessions		Cash Conventional	0		Cash Conventional	0		Cash Conventional	0
Location (City/Rural)	City - Good	Same	0		Same	0		Same	0
Leasehold/Fee Simple	Fee	Fee	0		Fee	0		Fee	0
Lot Size	160x150	80x150	+20,000		80x150	+20,000		80x150	+20,000
View	Typical	Typical	0		Typical	0		Typical	0
Design and Appeal	Typical	Typical	0		Typical	0		Typical	0
Quality of Construction	Good	Average	+20,000		Average	+20,000		Average	+20,000
Year Built	12 yrs ago	30 yrs ago	+20,000		30 yrs ago	+20,000		30 yrs ago	+20,000
Condition	Good	Average	+12,000		Average	+ 5,000		Average	+15,000
Above Grade	Total Bdrms Baths	Total Bdrms Baths			Total Bdrms Baths			Total Bdrms Baths	
Room Count	9 4 2.5	9 4 2	+ 1,000		9 4 2	+ 1,000		9 4 2	+ 1,000
Gross Living Area	2200 Sq. Ft.	2000 Sq. Ft.	+10,000		2200 Sq. Ft.	0		2,000 Sq. Ft.	+10,000
Basement & Finished Rooms Below Grade	N/A	N/A	0		N/A	0		N/A	0
Functional Utility	Typical	Typical	0		Typical	0		Typical	0
Heating/Cooling	Central HVAC	Central HVAC	0		Central HVAC	0		Central HVAC	0
Energy Efficient Items	Typical	Typical	0		Typical	0		Typical	0
Garage/Carport	2G	2 CP	0		2 CP	0		2 CP	0
Porches, Patio, Deck Fireplace(s), etc.	Porches, FP	Porches, FP	0		Porches, FP	0		Porches, FP	0
Fence, Pool, etc.	Fence, LS	Fence, LS	0		Fence, LS	0		Fence, LS	0
Other	Typical	Typical	0		Typical	0		Typical	0
Net Adj. (total)		☒ + ☐ -	\$ 83,000		☒ + ☐ -	\$ 66,000		☐ + ☐ -	\$ 86,000
Adjusted Sales Price of Comparable			\$295,000			\$290,000			\$300,000

The objective of this exercise is to demonstrate the adjustment process which can be utilized in conjunction with preparing a broker price opinion. The specific derivation of the respective adjustments is beyond the scope of this presentation.

This analysis is complicated by several factors, primarily the fact that the subject property is an over-improvement for its neighborhood. It is newer than the typical property, and is superior in quality of construction and condition. It has a larger site, as well.

Typically, for residential properties, there is a relatively significant amount of homogeneity between properties. This homogeneity is a result for the most part of zoning and subdivision restrictions, which have as their purpose the regulation of the type and intensity of property use. Conformity results from the effects of zoning and other regulation. Sometimes, however, there are instances where properties much larger than the surrounding properties, or of significantly better quality, etc., which complicates the analysis. Because these properties are not the norm, it is difficult to accurately measure the effects of the non-conformity. Take for example a residence with a double carport, and the property owner elects to enclose the carport and convert the space to living area. This action triggers a number of items of functional obsolescence. Since enclosed carports are relatively rare, there is little comparable data available at any point in time which would enable the analyst to isolate the obsolescence.

The subject case makes several points along this line. The subject is constructed on a larger site, resulting from combination of two lots. While the indicated value of a typical lot is \$30,000, does that mean that the subject's site is worth \$60,000, or something more or less.

The subject has a higher level of quality. The property owner consciously constructed a better house than others in the neighborhood for personal reasons. The effect of this is that, while the higher quality provides utility to the owner, a buyer may not be aware of, or be willing to pay for, the higher quality.

Differences in quality and condition are difficult to measure quantitatively. The primary point of the analysis presented herein is to show how the adjustments are applied to reach a value conclusion. Again, the analysis is complicated by the significant differences between subject and the respective comparables.

Imagine, on the other hand, if the subject would have been a 30-year original residence of standard quality and typical condition. Four of the comparable sales presented herein have those characteristics. These sales (1, 2, 3 and 5) provide a sale price per square foot range of \$104± to \$109± which is a relatively minor difference. In that instance, property pricing could easily be performed without the grid analysis.

The price opinion analysis can be performed for a number of different purposes. For real estate brokerage people, it is commonly utilized in order to provide a recommendation to a prospective seller. It has become somewhat common for price opinions to be utilized as an alternative to an appraisal. However, appraisal methods and techniques are necessarily used in such an analysis. A clear understanding of these methods and techniques is fundamental.

KEY RESPONSIBILITIES OF BROKER IN PRACTICE OF REAL ESTATE (BROKER RESPONSIBILITIES)

OBJECTIVES

As a licensed real estate broker in Louisiana you will have a wide range of responsibilities – to the agents you oversee, to the clients you serve, to the operation of the brokerage, to the governing regulations of the industry and many others. Upon completion of this lesson, you should be able to:

- Understand trust account requirements
- Adhere to fair housing laws
- Provide advertising that meets all regulations
- Supervise licensees with applicable commissions and fees
- Implement technology into your brokerage
- Understand antitrust laws
- Meet general ethical standards

TRUST ACCOUNTS

In this section we'll discuss trust accounts – what they are, their purpose and the type accounts brokers are required to setup.

We'll show who has ultimate responsibility for these accounts and wrap up the discussion with a look at the practice of commingling.

Definition

Trust fund accounts, or escrow accounts, are accounts a real estate brokerage will set up at a bank or some other financial institution.

These accounts are specifically for holding funds received by a broker or salesperson on behalf of a client (usually the buyer) and are held as part of the performance of any transaction for which a real estate license is required.

A resident broker, including corporations, partnerships and limited liability companies, who accepts any funds on behalf of clients in a real estate sales transaction shall open and maintain a **sales escrow checking account** in a financial institution in the state of Louisiana.

A resident broker, including corporations, partnerships and limited liability companies, engaged in the management of property owned by other persons shall open and maintain a **rental trust checking account** in a financial institution in the state of Louisiana.

A resident broker, including corporations, partnerships and limited liability companies, engaged in the collection of rental security or damage deposits in connection with property management activities on behalf of clients shall open a **security deposit trust checking account** in a financial institution in the state of Louisiana.

Per LREC rules the sponsoring broker shall have the authorized signatory responsibility on all trust accounts.

The addition of sponsored licensees and/or employees of the broker as signatories on the accounts shall not relieve the individual real estate broker of this responsibility.

Commingling

Is when a broker combines clients' funds with personal funds.

In most cases this is illegal and puts the broker's license at risk. There are a couple of exceptions:

1. A sum not to exceed \$2,500 may be kept in each sales escrow checking account, rental trust checking account, and security deposit trust checking account, which sum shall be specifically identified and deposited to cover bank service charges relating to the accounts, and shall not be used for any other purpose.
2. A broker engaged in property management activities may keep funds in excess of \$2,500 in a rental trust checking account for the temporary, limited, and specific purpose of enabling the broker to satisfy financial obligations for or on behalf of clients.

Fair Housing Laws

The basic premise on which federal and **Louisiana Fair Housing Acts** are built is simply this: all persons are entitled to live in the place of their choosing so long as they can afford to live there. Anything that we, as real estate licensees, do to prohibit this free choice is a fair housing violation. This applies to rentals as well as sales.

For this section we'll look at all aspects of Fair Housing Laws including, protected classes, covered transactions, exceptions, compliance, violations, enforcement and fair housing issues in advertising.

Protected Classes

There are seven classes of individuals who are protected by federal and state law from discrimination when purchasing a personal residence.

Those classes are:

1. Race
2. Religion
3. Color
4. National Origin
5. Sex
6. Handicap Status (disability)
7. Familial Status (children under the age of 18 living with parents or legal guardians, pregnant women and persons securing custody of children under 18)

If one individual discriminates against another, and the discrimination is found to be based on the second individual's membership in one or more of the protected classes, the individual committing the act(s) of discrimination may be found guilty and penalized under the federal and/or state fair housing acts.

Complaints against Louisiana (also: Arkansas, New Mexico, Oklahoma and Texas) licensees are filed with the Fort Worth Regional Office of the Department of Housing and Urban Development.

Let's look at a couple of real world examples.

A wheelchair-bound applicant for an apartment must have the kitchen and bathroom counters lowered in any unit he leases so that he will be able to live alone. He is willing and able to pay for the alterations he requires. The on-site manager at the apartment complex he likes refused to allow the alterations because "if I make alterations for you I'll have to let all the other residents make any alterations they want."

- a) The manager is correct, once he violates the apartment rules for one tenant he will have to allow all tenants the same privilege.
- b) The manager is incorrect. There are special rules for handicapped citizens that supersede apartment rules.

The answer is b. Under the Americans with Disabilities Act landlords must allow alterations to properties to accommodate the needs of handicapped tenants. This is one of the ways in which the Fair Housing Act requirement of not discriminating against persons based on handicap is accomplished

A Hindu couple is interested in purchasing a lot in a housing development being built just across the street from an evangelical church.

Pre-development sales in the development have been very brisk, with the majority of the lots selling to the church members.

- a) In the best interests of the Hindu couple, the sales-persons for the development should explain why they might not feel very comfortable in this neighborhood.
- b) Salespersons should not discuss religion with any persons who are interested in buying in this development.

The answer is b. Real estate licensees should not discuss religion with ANY customers or clients in association with ANY properties...

Covered Transactions

Except as covered under the exceptions listed on the next slide all real estate transactions including property listings, advertising, rentals or any other real estate activity must follow the requirements of the Fair Housing Laws.

The Louisiana Open Housing Act (La. R.S. 51:2601, et seq.) has been deemed substantially equivalent with the Federal Fair Housing Act.

Exceptions

In this course when the term “housing” is used it is important to remember that there are exceptions listed in the fair housing acts. These and only these are exempt:

1. Owner-occupied buildings with no more than 4 units
2. Single family housing sold or rented without the use of a broker
3. Housing operated by organizations for the use of members
4. Private clubs that limit occupancy to members

QUESTION:

Elderly Mr. Brown, had neither children nor any other living relatives. The last years of his life were eased by the congregation of his church, who cared for him and his home, making his last days as pleasant as possible. Mr. Brown willed all of his property to his church, including his personal residence and the five rental properties he owned. The congregation votes to restrict renters of these properties to members of the congregation.

Is this lawful under the fair housing acts?

- a. Yes, the congregation is exempt from the fair housing acts
- b. No, there are more than 4 units and Mr. Brown is not presently living in any of them

ANSWER:

The answer is a. The congregation is entitled to restrict the use of the housing to members of the congregation. This is one of the exemptions to the fair housing acts.

QUESTION:

Ms. Jones, a single lady, loves to dance but has reached an age where the number of dancing gentlemen is low. She lives in a Five-plex that she owns. To solve her problems, she decided to advertise the four rental units as “available ONLY to gentlemen over the age of 55 who love to dance and are willing to go dancing with the owner at least once each week.” Is this a lawful action?

- a) Yes. It's her home and she can rent to whoever she wants.
- b) No. She exceeds the number of units that would allow her the exemption for this action.

ANSWER:

The answer is b. Ms. Jones is not exempt from the fair housing acts because she is renting 4 units plus the one in which she is living.

The HUD Web Site

The HUD web site is your most up-to-date source for accurate information on the federal fair housing acts. If you learn to use it, you will never be accused of violating the fair housing acts because someone gave you incorrect or out-of-date information.

In the publications list you will find the whole of two pamphlets,
“Fair Housing: Equal Opportunity for All” and “Fair Housing—It’s Your Right.”

These two publications are free to read on the web site, download to your computer or print out. These are the publications that are given to the general public and include all information that any consumer will need to know to determine if they have been discriminated against. For that reason, they should be familiar to all real estate licensees who wish not to violate the fair housing acts.

Violations

Certain specific acts are prohibited under the fair housing acts if the intent to take these actions is based on membership in the protected classes. The acts as listed on the HUD web site are: [click>](#)

- Refusal to rent or sell
- Refusal to negotiate for housing
- Making housing unavailable
- Deny a dwelling (set different terms for persons in protected classes)
- Provide different housing services or facilities
- Falsely deny that housing is available for inspection, sale or rental

- For profit, persuade or try to persuade homeowners to sell or rent dwellings by suggesting that persons of a particular race or other protected class have moved or are about to move into the neighborhood (blockbusting)
- Deny any person access to, or membership or participation in, any organization, facility or service related to the sale or rental of dwellings, or discriminate against any person in the terms or conditions of such access, membership or participation
- Threaten, coerce, intimidate or interfere with anyone exercising a fair housing right or assisting others who exercise that right or make, print, or publish any statement, in connection with the sale or rental of a dwelling that indicates a preference, limitation or discrimination based on membership in a protected class.
- Make, print, or publish any statement, in connection with the sale or rental of a dwelling that indicates a preference, limitation or discrimination based on membership in a protected class.

The prohibition applies to single family and owner occupied housing that is otherwise exempt from the fair housing act.

Additionally, there is protection, over and above protection afforded by the above prohibited acts if you or someone associated with you has a mental or physical disability, a record of such a disability that substantially limits one or more major life activities; these disabilities include:

- Hearing, mobility and visual impairments
- Cancer
- Chronic mental illness
- AIDS or AIDS Related Complex
- Mental retardation

It is a violation of the fair housing acts to refuse to allow reasonable modifications to a dwelling or common use areas (at the expense of the renter or owner). It is also a violation to refuse to make reasonable accommodations in rules, policies, practices or services necessary for the disabled person to use the housing on an equal basis with nondisabled persons.

Let's look at some real world examples of some of these violations.

QUESTION:

In an attempt to fulfill the real estate licensees' duty of obedience to his client, a listing agent informs an African American couple that they cannot purchase a property because "it is right next door to the house where this property owner lives and he refuses to live next door to African Americans." The designated listing agent is fulfilling his legal obligation to the seller, therefore has not violated the fair housing acts.

- a) The seller and not the agent has violated the fair housing act.
- b) Both seller and agent violated the fair housing acts.
- c) No violation has occurred because the seller does not own more than four properties.

The correct answer is c. The seller is guilty of discrimination based on race. The designated listing agent is guilty of discrimination based on race. The licensee is not guilty of failing to render obedience to the seller because he must only obey the seller when directed to perform legal acts.

A designated listing agent presents an offer to a seller. The seller was visiting with a neighbor while his house was being shown and knows that the offer was made by an Hispanic couple. The seller rejects the offer rather than make a counter offer and tells the listing agent that if an offer is made by "real Americans" he will be glad to negotiate but if "those people" want to buy his property they will have to pay the full listed price with no concessions.

The listing agent should:

- a. Contact his broker to request that the listing be terminated.
- b. Inform the seller that the listing is terminated.
- c. Look for "real American" buyers.
- d. Report the seller to HUD.

The correct answer is a. Once the seller communicates his intention to violate the fair housing acts the broker is required to terminate the listing in writing.

The listing forms are complete except for the seller's signature. The seller, a Viet Nam veteran, looks the listing agent right in the eye and states that his property can be shown to anyone except "gooks" and if any come onto his property he will shoot first and ask questions later. He further states that he is aware of the fair housing acts but does not accept them as binding.

The listing agent should:

- a. Thank the seller for his service to the country and honor his wishes
- b. Thank the seller for his service to the country but refuse the listing

The correct answer is b. The seller is in violation of the fair housing acts and is attempting to place the listing agent in violation also.

The seller of a property directs his listing agent to use a code word when calling for an appointment to show his property to members of a certain ethnic group. If the code word is used, the appointment will be denied.

Is this a violation of the fair housing acts?

- a. Yes. The purpose of the code word is to discriminate against members of a named ethnic group.
- b. No. The prospective buyers will never know about the code word and are therefore unlikely to be offended by its use.

The correct answer is a. Whether or not the person who is being discriminated against knows there is discrimination is not the test under the fair housing acts.

Enforcement

Enforcement of the Fair Housing Act is by the Louisiana Department of Justice, which may receive complaints directly from individual citizens or by referral from the department of Housing and Urban Development (HUD) of the federal government.

HUD investigates complaints of housing discrimination based on race, color, religion, national origin, sex, disability, or familial status. At no cost to the complainant, HUD will investigate the complaint and try to conciliate the matter with both parties

If the complaint is found to have merit, it is often turned over to the state for further actions. At this time the Louisiana Open Housing Act governs the proceedings.

Recall that one of the Fair Housing violations was:

Make, print, or publish any statement, in connection with the sale or rental of a dwelling that indicates a preference, limitation or discrimination based on membership in a protected class.

Make sure your agents understand and follow all advertising policies regarding the Fair Housing Act. Any slight indication or interpretation of discrimination whether blatant or even implied and should always be avoided. Stick to selling the features of the properties and you'll be fine.

Advertising

In this section we will look at the basic requirements for real estate advertising – who has ultimate responsibility for agency advertising; what constitutes misleading or incorrect statements.

We'll discuss the difference between uniformed and deliberate misrepresentation.

Lastly, we'll have a brief look at using Social Media as the New Medium.

Responsibility for advertising

In all cases the designated qualifying broker is responsible for all aspects of agency and listings advertising.

That's not to say the broker has to physically look at and approve every advertising order that goes out the door. If you have a good staff that you trust, hopefully you won't have to.

It just means that if an agent under your supervision happens to put out some misleading advertising you own it and could be held accountable for the ramifications.

All advertising must include the business name recorded with the commission.

A group or team name may be used in an advertisement only with the approval of the sponsoring broker.

Any person listed as a group or team member in the advertisement must be a licensee sponsored by the sponsoring broker.

Misleading/Incorrect Advertising vs. Puffing

Misleading or non-factual advertising is making statements in advertising known to be false.

For example, if a property was 980 square feet and you intentionally listed it at 1,050 square feet so it would be over 1,000, is misleading and considered fraud. This is a serious violation and risks license revocation.

Puffing is an exaggeration of a personal opinion.

For example an agent might put out an advertisement for a new home that reads:

“The best kitchen I have ever seen!”

This statement is simply a matter of opinion and not a presentation of fact. This kind of advertising is done frequently. Puffing might be considered a bit unprofessional but it is not illegal, where intentional misrepresentation is.

Uninformed misrepresentation occurs when a licensee falsely states something as fact that he should know.

Deliberate or misrepresentation is when the licensee knows a statement is false but states it anyway, with an intention to improperly influence another.

For example: A buyer wants to buy a home where he can also setup a dog grooming service. The agent finds a property where the existing owner already has a Barber Shop which looks like it is a perfect fit for the buyer and informs the buyer the zoning should also cover the dog grooming service.

The buyer purchases the home but when he applies for the business license he is denied because the zoning excludes all forms of animal related businesses.

The agent should have known the specifics of the zoning law but there was really no intent to deceive.

If he knew it was an issue but told the buyer otherwise simply to close the sale, then he likely crossed the line into deliberate misrepresentation.

What is Social Media?

If “media” is considered a device for communication, such as newspaper or radio, then “social media” would be a social method of communication.

One of Webster’s definitions for “Social” is “living or disposed to live in companionship with others or in a community, rather than in isolation” – which means it’s simple human behavior to closely interact with each other.

Social media has joined us together at a community or even worldwide level like no other time in history.

Social media used for real estate purposes is how we can closely inform and interact with potential home sellers and buyers.

The key part of that is interact – we can directly communicate with and market to a vast pool of buyers and sellers.

Facebook

Facebook is a social networking website that enables users to connect and share with family and friends.

Facebook serves almost 1.5 billion users monthly.

For broker marketing today a Facebook presence is essential.

A solid Facebook strategy will allow you to:

- Highlight listings
- Post Open House events
- Contests/Sweepstakes
- Geo-Targeted Ads
- Market engagement

Twitter

Twitter is a social networking service where users send and read short 140-character messages called “tweets”.

The 2014 estimate for active tweets was over 500 million daily.

Twitter can still be used to market specific property even with such a short message format.

Because a Tweet is limited to 140 characters you have to be very creative in condensing content. Think of Twitter as your personal contact market place. You want to cultivate relationships by being friendly and informative while actively marketing your brokerage. So, think about...

- Personal marketing
- Tips and news blurbs
- Questions and answers
- 80/20 rule – Lifestyle/Listings

YouTube

YouTube is a video-sharing website that allows users to upload, view, and share videos. Launched in 2005 it has become the web's premier destination for video.

By March 2015, YouTube members have produced over 10,000 videos that have produced 1 billion views and 70+ million hours of watch time.

- Property walk-throughs
- Drives brand awareness
- Platform for premier visuals
- Unified team message

According to the National Association of Realtors, more than 50% of prospective home buyers use YouTube as their primary video research tool. Video marketing is a proven strategy among top brokerages everywhere.

Pinterest

Pinterest is a web company which operating a photo sharing website. Founder Ben Silbermann, summarized Pinterest as a "catalog of ideas," rather than as a social network.

The 4th largest social site is all about connecting through images. Since listings are sold through a mostly visual connection this is a match made in heaven.

Set up Pinterest boards for your community, lifestyles, home décor and your listings.

Again, apply the 80/20 rule. Let your listings blend into the social aspects of the site by limiting them to 20% of your overall content.

Social Media Tips

1. Don't spread too thin. Pick two platforms for your marketing focus.

Don't try to be everything to everybody. Social media marketing demands focus and perseverance. Pick two platforms and build those into a strong presence.

2. Blend social content with property ads – 80/20

Make your platform a social experience by providing a source of entertaining and informative content as the anchor for your ads.

3. Consider a blog strategy to grow followers and gather consumer information.

Blogging is a proven strategy to build a personal presence while gathering consumer information. The trick is to be consistent and be in for the long haul.

4. Collaborate with a social media marketing pro.

Marketing is the life-blood of your brokerage and should not be left to chance. For your social media strategy, unless you have long term experience developing a social strategy, do-it-yourself is not recommended simply because it's too important to learn-on-the-job. Your chance of success is much greater working with a professional than taking on the role yourself.

In this section we'll take a look at the broker's role as a supervisor – what your responsibilities and liabilities are with regards to agents under your direct supervision. We'll also discuss your obligation to train and supervise the agents under your license. We'll wrap up the section by exploring the difference between an employee and an independent contractor.

Liability/Responsibility

As a sponsoring broker you are legally responsible for the real estate activities of your agents.

The statute reads: Active licensed brokers who elect to sponsor an applicant for a real estate license shall be subject to the duties and penalties prescribed for sponsoring brokers in the Louisiana Real Estate License Law and commission rules and regulations and shall bear the responsibility for the license activity of any sponsored licensee.

Subject to investigative results the sponsoring broker can be fined accordingly or lose their license because of the misdeeds of an agent.

Responsibility to Train and Supervise

Building a successful brokerage requires several components, including a comprehensive training strategy.

Coaching agents new to the business and building on the experience of your top producers with dedicated training should be an integral part of your brokerage strategy. Effectiveness in the marketplace comes by staying current with real estate laws, listing management techniques, sales strategies and other topics integral to brokerage growth and success.

Your role as the supervising broker is more like being a sports coach. Your role is to motivate your team, build strategy, set goals and guide your agents to success.

The financial health of the brokerage is the ultimate responsibility of the business leader, usually the broker in charge. Setting and implementing policy, talent acquisition and disposition, training, coaching, and other operational activities should align with fiscal goals.

Independent Contractors vs. Employees

Real estate salespeople may be considered independent contractors or employees.

The difference between the two essentially comes down to is how much control a broker exerts on an agent.

For example, if you set specific hours or and/or a specific place for the agent to perform his duties, or you place expectations on the contractor to attend staff meetings, you may be placing the independent contractor status at risk.

It is important to understand the characteristics and contrasting features of an independent contractor versus an employee.

According to the Tax Equity and Fiscal Responsibility Act of 1982, a statutory non-employee (*Independent Contractor*) must satisfy the following guidelines:

- A current real estate license
- A written agreement with the broker detailing an independent contractor relationship

That's the Independent Contractor Contract which should be executed annually and reflect the day-to-day working conditions and expectations in the terms of the contract.

- Compensation must be based on productivity not hours worked (At least 90%)

Independent Contractors vs. Employees

Brokers have more control and authority over employees.

Federal withholding and FICA fees must be deducted from the employee's commission payments.

FICA matching must occur and payment into the state unemployment fund must occur.

Other employment benefits, insurance, overtime, vacation pay or more bring additional cost.

Some other distinctions between independent contractors and employees include:

ITEM	INDEPENDENT CONTRACTORS	EMPLOYEES
Written Contract:	Required	Optional
Broker Control:	Little	Full
Training:	Voluntary	Required
Office Space:	Voluntary	Provided
Marketing:	Pays	Does Not pay
Secretarial Services:	Optional	Provided
Floor Time:	Voluntary	Required
Staff Meetings:	Voluntary	Required
Salary or Draw:	No	Yes
Expense Accounts:	No	Optional
Fringe Benefits:	No	Optional

They say money doesn't make the world go round. To that I would add, but it sure greases the wheel. Disputes over commissions and fees are a common happening in this business. Anything you can do to eliminate or at least alleviate these arguments is in your best interest.

Over the next few slides we'll take a look at things in place to help reduce agent and broker disputes about commissions and fees.

Procuring clause

A procuring cause is the interaction between a home buyer and a real estate agent.

When a home buyer has worked with multiple real estate agents while looking for a home, most will feel entitled to a commission

The agent who ultimately caused the buyer to purchase the home and earned the commission is generally the procuring cause agent.

The best way to avoid "*procuring cause*" disputes is by asking home buyers to sign a buyer's agency agreement.

The agreement should stipulate that the buyer's agent is entitled to the commission when the sale closes.

Your agents should always ask new clients if they're currently working with another agent if only to make sure the commission goes to the right person. Avoid taking on a client who already signed a buyer's agency agreement with another brokerage.

Referrals

The essence of a referral is simply a recommendation. In best case it is a high quality lead likely to end with a real estate closing.

Referral fees are common in the industry. Some real estate organizations business models are based solely on referral income.

Finder's Fee

Much like a referral fee, a finder's fee is a reward to someone for bringing a deal to an agent.

While these fees may be allowed in other jurisdictions, they are not allowed in Louisiana.

It goes back to the law. Unless someone is licensed by the real estate commission they cannot receive a commission for selling real estate. Any referral fee can only be received by a licensed agent or broker.

Use of Technology

Over the last couple of decades, the real estate industry has seen a major shift in the way properties are marketed, home buyers seek out their next home and how property sales close. Technology has driven this change.

In this section we'll discuss the advent of electronic signatures and document delivery in this internet age. We'll go over some legal requirements for internet advertising and wrap up the section with a look at MLS data exchange.

Electronic Signature

An electronic signature is a digital means indicating one of two things:

- It certifies that the sender adopts the contents of an electronic message.
- The person claiming to have written a message is the one who wrote it.

In essence it's a digital seal that validates the equivalence of a handwritten signature.

The U.S. Code defines an electronic signature for the purpose of US law as "an electronic sound, symbol, or process, attached to or logically associated with a contract or other record and executed or adopted by a person with the intent to sign the record."

At all levels of government and private business, e-signatures are becoming increasingly viable as a form of legal certification.

With the Uniform Electronic Transactions Act (UETA) in most states and the Electronic Signatures in Global and National Commerce Act (ESIGN) in 2000, the use of electronic records signatures in real estate was finally decided.

Both sets of regulations establish the principle of equivalence and confirm that digital signatures carry the same legal substance as paper documents and handwritten signatures.

There are specific Rules of General Validity that must be considered:

1. A document or signature cannot be denied legal effect or enforceability solely because it is in electronic form.
2. A contract cannot be denied legal effect or enforceability solely because an electronic record was used in its formation.
3. If a law requires that a record be in writing, then an electronic record satisfies the law.
4. If a law requires a signature, then an electronic signature satisfies the law.

As brokerage leaders you should define document control policies and procedures that satisfy the needs of your business and the interests of your clients.

Document Delivery

The most challenging part of a real estate transaction is the paperwork.

At a real estate closing a buyer will dot enough I's and cross enough T's to last a lifetime. You and your team can ease the pain of the process by insuring the document package is complete, without errors and delivered on-time.

Document delivery services are in business solely to help you do that. Leveraging the power of technology, a service can provide error free documentation delivered to the proper destination, on-time and totally legal.

Seek out a solid document delivery service and partner up for the paperwork. People do business with people that are easy to do with. As you get a reputation for solid documentation your market position will benefit.

Internet Advertising

There are four sections of the rules regarding internet advertising:

1. A real estate broker advertising or marketing on a site on the Internet must include the following data on each page of the site on which the advertisement appears:
 - a. The broker's name or trade name
 - b. Main office city and state
 - c. Regulatory jurisdiction of license
2. Emails, discussion groups or other internet mechanisms used for marketing communication must include on first or last page of all communications:
 - a. The broker's name or trade name
 - b. Main office city and state
 - c. Regulatory jurisdiction of license
3. An associate broker or salesperson marketing on the Internet must include at any location where the licensee's advertisement appears:
 - a. Associate broker or salesperson's name
 - b. The broker's name or trade name
 - c. Main office city and state
 - d. Regulatory jurisdiction of license
4. Associate brokers or salespersons using emails, discussion groups or other internet mechanisms used for marketing communication must include on first or last page of all communications:
 - a. Associate broker or salesperson's name
 - b. The broker's name or trade name
 - c. Main office city and state
 - d. Regulatory jurisdiction of license

Data Exchange (MLS)

A Multiple Listing Service (MLS) essentially brings real estate brokers and agents, buyers and sellers together.

The MLS facilitates cooperation between broker participants and provides an organized platform for listing properties to better serve broker's clients, customers and the public.

The listing data stored in a multiple listing service's database is the proprietary information of the broker who has obtained a listing agreement with a property's seller.

Membership in an MLS is not a legal requirement for the practice of real estate brokerage, however without membership in an MLS covering your market, your access to other listings will likely be somewhat limited.

Brokerages are leveraging technology by using the Internet Data Exchange (IDX) aspect of MLS.

This allows MLS members to share each other's listings on each other's websites. It's a mutually beneficial marketing arrangement that allows for a wide marketing presence for listings.

The National Association of Realtors® (NAR), has mandated the IDX policy regarding implementation, use and control of the data exchange.

The policy is extensive and outside the purpose of this training. We are providing a copy of this policy you should have familiarity with as you set your own data exchange programs in place.

Antitrust Laws

Starting with the Sherman Antitrust Act, enacted in 1890, the U.S. Government has taken a strong stand in the protection of consumer from unscrupulous business tactics that may unfairly target consumers.

Purpose

In short anti-trust laws are designed to prevent monopolies and unfair trade practices that reduces competition.

Business practices and behaviors which violate antitrust laws include collusion, price fixing, market allocation, bid rigging, restricting market entry, exclusive dealing, and predatory pricing.

These laws are applied to a wide range of questionable business practices and industries.

History

Enacted in 1890, the **Sherman Antitrust Act** prohibits restraint of interstate and foreign trade by conspiracy, monopolistic practice, and certain forms of business combinations, or mergers.

The Sherman Act empowers the federal government to proceed against antitrust violators.

The Clayton Antitrust Act of 1914 reinforces and broadens the provisions of the Sherman Act.

Among its prohibitions are certain exclusive contracts, predatory price cutting to eliminate competitors, and interrelated boards of directors and stock holdings between same-industry corporations.

The Clayton Act also legalizes certain labor strikes, picketing, and boycotts.

Potential Violations in Real Estate Practice

Collusion – the illegal practice of two or more businesses joining forces or making joint decisions which have the effect of putting another business at a competitive disadvantage.

Businesses may not collude to fix prices, allocate markets, create monopolies, or otherwise interfere with free market operations.

There are dozens of mortgage fraud, application falsification, equity skimming, short sales and other huckster schemes involving collusion that represent billions of dollars in fraudulent loans every year. With advances in fraud detection technology the chances of getting caught have never been greater.

Price Fixing – Price fixing is the practice of two or more brokers agreeing to charge certain commission rates or fees for their services, regardless of market conditions or competitors.

Such pricing avoids and disturbs the dynamics of a free, open market.

For instance, the two largest brokerages in a market jointly decide to cut commission rates by 50% in order to draw clients away from competitors. The cut-rate pricing could destroy smaller agencies that lack the staying power of the large companies.

Market allocation – the practice of colluding to restrict competitive activity in portions of a market in exchange for a reciprocal restriction from a competitor:

"We won't compete against you here if you won't compete against us there."

For example, Broker A agrees to trade only in single family re-sales, provided that Broker B agrees to focus exclusively on apartment rentals and condominium sales. The net effect is an illegally restricted market where collusion and monopoly supplant market forces.

Violations of fair trade and anti-trust laws may be treated as felonies, and penalties can be substantial. Loss of one's license is also at stake. Brokers are well-advised to understand and recognize these laws.

General Ethics

Jazz trumpeter Wynton Marsalis once said: Ethics are more important than laws.

Without ethics and personal accountability, we couldn't have any trust in anybody. Imagine trying to do business in that world.

So what are ethics? Ethics is a personal philosophy around the concepts of right and wrong conduct. It's the principles we live by.

Stellar ethics are crucial in our industry. This is a trust business and essential for building relationships with the people you will need to be successful.

And the other side of the coin is – under certain circumstances, questionable ethics could land you in jail.

In this section we'll look at the importance of ethics at your brokerage.

Practicing Within Area of Competence

Article 11 of the Realtor® Code of Ethics says in part:

The services which REALTORS® provide to their clients and customers shall conform to the standards of practice and competence which are reasonably expected in the specific real estate disciplines in which they engage".

Clint Eastwood said – "A man's got to know his limitations."

In this business you must know, and stick to, your area of competence.

For example, if you have spent 20 years as a property manager and then accept a position as a commercial property broker, you will be out of your element and could easily be put in a position to advise a client on a topic you have no knowledge of.

Since you are bound by commission rules to act in the best interest of your clients, acting from a position of ignorance is unethical at best, unlawful at worst.

Avoiding unauthorized Practice of Law and Accounting

In short, if you don't have a license to practice law you cannot provide any legal services.

Only lawyers can:

- Initiate a lawyer-client relationship
- Provide legal advice
- Sign legal papers on behalf of a client
- Carry out legal proceedings in court
- Charge a fee for legal services

So as an agent or broker you cannot legally explain the legalities of preprinted contract clauses to a buyer or seller. You cannot add additional language to contracts or in any way alter the legal specifics of a contract.

The key to avoiding the unauthorized practice of law in Louisiana is to educate yourself. Know what defines a lawyer actions in Louisiana. See the resource document "Louisiana Lawyer definition" for more information.

Article 13 of the Realtor® Code of Ethics states: *shall not engage in activities that constitute the unauthorized practice of law and shall recommend that legal counsel be obtained when the interest of any party to the transaction requires it.*

The same holds true for accounting services. Because the State licenses Certified Public Accountants, the practice of accounting without a license is unlawful.

There are very specific educational, testing, experience, legal and character requirements to obtain a CPA license to practice in Louisiana. If you are performing services that normally demand the services of a CPA then you are likely in violation of law.

To avoid legal entanglements, you should make use of a local accounting firm to do these kinds of activities.

Real Estate Trade Organizations

As a broker you should take advantage of trade organization membership that focuses on your chosen field of expertise.

This is a small sampling of a few you may decide to join. Ethics in real estate will be a focus topic for any of these.

There are many others. Look for the Real Estate Trade Organizations in the Resources folder.

TECHNOLOGY IN REAL ESTATE

INTRODUCTION

Real estate professionals can rest easy knowing that their industry satisfies a primary need; in essence people must have a place to live and in most cases a place to conduct business. There are many jobs and in some cases entire industries that cannot state that fact because of factors such as outsourcing, offshoring, or structural unemployment. Outsourcing of course is when a product or service is eliminated within an organization and the product or service is procured using an external organization, such as eliminating a marketing division of the organization and hiring an outside marketing or advertising agency. Offshoring is when the product or service is taken to another country, but even with the concern that these concepts cause, the most disturbing is structural unemployment. Structural unemployment is when a person's job is lost because the job doesn't exist anymore. I can only imagine the thoughts that went through the heads of stage coach companies when Carl Benz invented the modern automobile and then Henry Ford figured out how to mass produce them, until that point besides the use of trains, it was horses or stage coaches, but as transportation evolved, the needs for those forms of transportation became antiquated. That is what structural unemployment is, it's when your job or profession doesn't exist anymore because of a better solution or some cases, minimal or no demand.

As a licensed real estate professional, there could be instances when you lose your job, but the need for real estate professionals is ever present and growing. You don't have to worry about the real estate industry becoming extinct but as a real estate professional, if you are not proficient with technology, then you may become extinct. You are living in a digital age in which the use of email, mobile applications (apps), digital agreements/contracts/disclosures, digital signatures, and internet based marketing are necessities. If you enter the real estate industry and are not technology proficient, then you will become structurally unemployed. Employers will not want to hire you if you are not familiar with everyday technologies. In essence, don't apply if you can't use technology.

For the most part this will be a non-issue for Generation Y and beyond, especially those born in the later years of this generation, they haven't lived without technology, but for earlier generations including Generation X, technology or the use thereof can be a troublesome issue. With the advent of the Internet, society started sharing information in ways that never occurred before, and now that the technology infrastructure has caught up with information sharing ingenuity, the way you do things both personally and professionally has now been changed forever.

Even though it seems you cannot remember a time when the Internet was not present, it wasn't that long ago. The World Wide Web was created between 1989 & 1990 and estimates state that by 1993 there were just over 100 websites on the Internet. Popular search engines like Yahoo were founded in 1995 and Google in 1998. It's amazing how in that short time, technology has changed and the Internet has grown. According to most sources there are well over 600 million active websites on the Internet and the use of technology has infiltrated every aspect of daily life. From personal email to shopping, and everywhere in between, technology is present. As a real estate professional, you will see it doesn't stop with shopping for real estate. According to realtor.com, 90% of homebuyers use the Internet during the buying process. With that said, the writing on the wall should be very clear. As a real estate professional, you MUST not only be familiar with technology, but you MUST be proficient with technology in order to succeed. If you think you are going to start a career in real estate and are not functionally competent with technology and have no desire to work on proficiency, then simply put, you will not make it. I know that sounds harsh, but it is reality.

In the next few sections, you will focus on gaining an understanding of technology in the real estate industry. You will review industry regulations as they relate to technology, social media, technological resources, technological tools, and how business is being created and conducted through technology.

INDUSTRY REGULATIONS

It is important to be aware of industry regulations that impact licensees; in this section a cursory review will be made of regulations associated with the use of technology in the real estate industry. There are many other regulations, but these regulations are ones that every licensee should be aware of and have a general understanding.

ESIGN Act

The Electronic Signatures in Global and National Commerce Act or the ESIGN Act as it is known, is a federal law enacted into law in 2000 that legalized the use of electronic signatures and records. Individual states have laws pertaining to digital or electronic signatures, but this federal law effectively legalized the usage of electronic signatures and records on an interstate basis. There are also parameters of this law that deal with foreign commerce as it relates to these topical areas. After the passage of this law, parties to a contract may elect to digitally sign a document and that electronic signature carries the same weight as a signature executed with pen and paper. An electronic signature may be as simple as a party to the contract typing their initials and name using a keyboard. Today there are a variety of companies that provide esignature services which allow users to sign documents online without having to print, sign, scan, and email the document. This saves time and money when executing agreements. I will discuss these types of services in the **Web Tools** section of the course.

Louisiana Real Estate Commission Rules and Regulations

The Louisiana Real Estate Rules and Regulations expressly states the rules as it relates to the usage of electronic communication and Internet advertising. As a licensee, it is imperative that you be knowledgeable of these rules and regulations in order to maintain compliance as you use technology.

Chapter 2515 of the Louisiana Real Estate Commission's Rules and Regulations states the following:

- A. A real estate broker advertising or marketing on a site on the Internet must include the following data on each page of the site on which the advertisement appears:
 - 1. the broker's name or trade name as registered with the commission;
 - 2. the city and state in which the broker's main office or branch office is located.
 - 3. the regulatory jurisdiction(s) in which the broker holds a real estate brokerage license.

- B. A real estate broker using any Internet electronic communication for advertising or marketing, including but not limited to, e-mail, email discussion groups, and bulletin boards, must include the following data on the first or last page of all communications:
 - 1. the broker's name or trade name as registered with the commission;
 - 2. the city and state in which the broker's main office or branch office is located.
 - 3. the regulatory jurisdiction(s) in which the broker holds a real estate brokerage license.

- C. An associate broker or salesperson advertising or marketing on a site on the Internet must include the following data on each page of the site on which the licensee's advertisement or information appears:
1. the associate broker's or salesperson's name;
 2. the name or trade name of the licensed broker or agency listed on the license of the salesperson or associate broker;
 3. the city and state in which the broker's main office or branch office is located.
 4. the regulatory jurisdiction(s) in which the broker holds a real estate brokerage license.
- D. An associate broker or salesperson using any Internet electronic communication for advertising or marketing, included but not limited to, e-mail, email discussion groups, and bulletin boards, must include the following data on the first or last page of all communications:
1. the associate broker's or salesperson's name;
 2. the name or trade name of the licensed broker or agency listed on the license of the salesperson or associate broker;
 3. the city and state in which the broker's main office or branch office is located.
 4. the regulatory jurisdiction(s) in which the broker holds a real estate brokerage license.

If a licensee, using Internet advertising and/or electronic communication as stated in Chapter 2515 and does not adhere to the requirements set forth in the rules and regulations, then the licensee will be subject to disciplinary action by the Louisiana Real Estate Commission.

Furthermore, the Louisiana Real Estate License Law states that licensed brokers must maintain records for a period of 5 years, and with the Louisiana Real Estate Commission's approval those records may be kept in a digital format thus eliminating the need for paper records.

SOCIAL MEDIA

Social media is a means whereby people interact through the Internet in which they create and share data with each other; effectively, forming web based communities that allow people to stay connected with each other. Web sites such as Facebook®, LinkedIn®, and Twitter® are all forms of social media that are available to users; although, there are many more, these are the most popular social media sites. Social media plays a pivotal role in both personal and business relationships and networks. In fact, Social Media allows a person to incorporate their personal contacts into their business network and the forum that social media displays are unprecedented in terms of reach and availability to potential clients.

As a real estate professional, the use of social media can be vital to your career. At no other time in history have we had the capacity with the click of a mouse to market to hundreds and even thousands of potential clients. By informing your personal network of your profession, you have now directly marketed to your personal network in the most time and cost efficient means available in the market. Using Facebook® as an example, your friend Joe whom you have not seen in person since high school now becomes a potential client with a simple post. One of the most frustrating situations for real estate professionals is when you find out that a friend or family member (a member of your personal network) was a party to a real estate transaction and you were not involved; with the use of social media, these type situations can be minimized or even eliminated because you now have access to your personal network on a 24/7 basis. In this section, we are going to define and explore opportunities with the use of Facebook®, LinkedIn®, and Twitter®.

Facebook®

Facebook® is the most recognizable brand of social media, with current estimates of over one billion users, it is also the largest. To put that in perspective, one in seven people on the planet have a Facebook® account. Although, most people are very familiar with Facebook®, it is effectively a web based community in which users can network with one another. Facebook® users can "friend request" other users to add to their network, and after the other user accepts the "friend request", they will be added to your network. As a user makes a post, it will appear on the home page of each user in your network. There are also other tools such as private

messaging and chat that allows users to interact. With the number of users, and the capacity to access everyone in your network with a single post, Facebook® has become one of the most powerful tools available for networking, and it is a free service. As you build your Facebook® network, it is important to stay active with new posts in order for users in your network to feel connected to you.

Because of the nature of the real estate industry, Facebook® is extremely effective in terms of networking and marketing. The introduction of the **Social Media** section makes the case for networking; as you build your network, you can make real estate and professional posts in order to make certain that your network identifies you as a real estate professional because as stated in the introduction to this section there is nothing worse than to lose a sale that you should have procured because a friend, family member, or acquaintance does not identify you as a real estate professional when needing real estate services. Part of the identification process is also marketing. As a real estate professional make posts including information about your listings, because this allows you to reach a segment of the market with property information and it continues to reiterate the identification process of you as a licensed real estate professional. This isn't solely for new licensees, licensed real estate professionals who have been in the industry for many years can also benefit from social media networking because new relationships are constantly being forged and you are also in social settings in which other people may know you through charitable organization, religious affiliations, children's activities, etc., and never know your profession. Facebook allows you to identify yourself in a professional capacity.

Another benefit to marketing on Facebook® is that it is free, just like with joining the service. When I say free, I am speaking with regard to making posts or a professional page separate from your individual page, if you choose to do so. Facebook® does offer paid advertisements in which you can pay to market yourself to a very direct market; for example, a certain town or parish. On the side of a user's page are advertising spots, and you could pay to purchase one of them. As print media costs continue to rise and become less effective, Facebook® offers either an alternative or a complementary tool in your marketing portfolio that you may offer to clients. Furthermore, in the digital age in which we work and live, you must have a digital marketing portfolio or you will lose listings and other business. The negative of Facebook® is that you are limited to marketing to your network unless you pay to advertise. So, although effective for both networking and marketing, because of the nature of this social media site, it is definitely more effective for networking than marketing, but do not underestimate the site's marketing worth even with just maintaining a free marketing strategy.

Linkedin®

Linkedin® is a social networking web site for professionals; unlike the broad Facebook membership, Linkedin® is designed for professional networking and whereas Facebook® refers to other users in your network as friends, Linkedin uses the name "contacts". Linkedin® allows users to develop a profile based on professional experience and then allow contacts in your network to endorse your skillset. Also in similar fashion to Facebook, Linkedin® users can make post to their page. Linkedin® allows its users to search for available jobs within their network and it allows users to procure endorsements from other contacts in their network. Linkedin® also has an interests tab that allows users to stay informed regarding certain companies, join and interact with specific groups, and through what it refers to as "influencers" allows users to stay informed about areas of interests.

As a real estate professional, Linkedin® can be very important because it allows new and experienced licensees to form and build relationships with other licensees, lending professionals, title professionals, insurance professionals, legal professionals, potential clients, and other contacts important to the practice of real estate.

Twitter®

Twitter® is a social networking service that allows its users to send text messages that consists of no more than 140 characters. These text messages or mini blogs if you will are referred to as tweets. As of 2012, Twitter® states that it has over 500 million registered users that generate over 340 million daily tweets. When a user tweets a message, his or her followers will see the post and if so desired tweet back. Twitter® is different from Facebook® and Linkedin® in that its focused interaction between its users is very specific by posting tweets and not broad based in its approach to facilitate social interaction.

As a real estate professional, you should build your professional network with colleagues, service providers (lenders, title companies, etc.), friends, acquaintances, and potential clients (which could include friends and acquaintances). Twitter® can be helpful to real estate professionals by posting mini blogs regarding industry news, opinions, events (such as open houses), or current events as well as new listings and property updates.

By posting a tweet, you can provide valuable information to your followers without tying up a tremendous amount of your time.

TECHNOLOGICAL RESOURCES

There are many web sites on the Internet that can assist licensees with the daily practice of real estate. Some of these sites are equally as useful to consumers who are entering the market place as buyers and sellers. As I stated earlier, according to realtor.com, 90% of buyers use the Internet when purchasing a home. That is an incredible statistic and because of that demand in the marketplace, there are many real estate web sites that can be used as a resource for licensees and consumers alike. In this section, I will discuss Trulia®, Zillow®, and realtor.com, which are a few of the more popular real estate web sites on the Internet.

Trulia®

Trulia® is a public traded company that through their web site and mobile application allows users to perform property searches and procure additional data; it states that it currently has over 31 million visitors per month and according to the web site many of its visitors have not enlisted the assistance of a real estate professional. Trulia® provides data for both real estate sale and rental markets. Consumers can search available listings and in addition to search results, consumers can view data regarding schools with ratings, crime reports, and sales data. Real estate professionals can enter their listings for free, but Trulia also offers packages that real estate professionals can purchase which provide additional services such as ad free “featured listings” and sales lead information. Real estate professionals can also place local advertisements which can be viewed within specific geographic searches and mobile advertisements are also available. Currently, all properties available on Trulia® only come from real estate professionals and/or professional organizations (MLS), individual homeowners (FSBO’s) cannot post properties on the web site. Trulia® draws its property information from a variety of different sources, such as salespersons, brokers, and MLS services; and other services such as mapping from Google, crime statistics from partnering web sites including crimereports.com and everyblock.com, and sales information from a variety of sources including public data. It is important to state that web sites such as Trulia® are a good resource but as a real estate professional, always double check information before relying on it. Because of the way that search data is generated, for example using zip codes, information such as property values can be inconsistent and inaccurate.

Zillow®

Zillow® is another web site with accompanying mobile application that is geared toward the real estate industry in which users can search for available properties (both on a “for sale” and “rental” basis), research property values referred to as Zestimates®, procure local information, ask real estate advice, and research competing mortgage companies. Currently, Zillow® states that it has data on over 100 million properties throughout the United States. Like Trulia®, Zillow® offers real estate professionals’ fee based packages to spotlight them and to provide access to additional services. Unlike Trulia®, Zillow® allows individual homeowners (FSBO’s) to upload properties to the site. Zillow® also allows users to research property value trends for a specific property across an incremental period of time. As with Trulia® or any other web site that provides valuation services, be cautious, because there can be flaws in the formula. Zillow® like other competing sites is quick to point out, that their valuation services are not appraisals and should not be viewed as such, but rather as a tool to assist real estate professionals and homeowners with information for a specific property or area. Typically, the valuation formulas used by these web sites includes tax information from public records, sales information, and even input from users; with that said, users can enter inaccurate information and property tax assessment data can be a serviceable source but can still be flawed with regard to wrong or outdated assessments. Overall, real estate professionals should view sites such as Zillow® and Trulia® as a tremendous source of information and potentially as a tool in their marketing plan, just remember they have limitations.

Realtor.com

Realtor.com is a web site with accompanying mobile application that is owned and operated by the National Association of Realtors (NAR). It is the most complete collection of available properties on the Internet because the web site procures listings from all partner multiple listing services (MLS) nationwide. As realtors® enter new

listings (for sale or rentals) into their local multiple listing services, they are automatically uploaded to realtor.com. According to realtor.com, it is the most visited real estate web site on the Internet. Because it is owned by the National Association of Realtors, only member real estate professionals can have listings available on realtor.com, not for sale by owners (FSBO's) nor non-member real estate professionals can market through this site and because of its design for adding new listings through local multiple listing services, realtor.com's data is very accurate. Like other real estate web sites, realtor.com offers information on a variety of real estate topics including but not limited to housing data (sold information, foreclosures, etc..), advice (such as pointers on moving), market data (average sales prices in a specific area, number of houses available for sale, etc..) and mortgage information. Realtor.com also offers fee based packages for realtors®, which provide additional services and data.

WEB BASED BUSINESS OPPORTUNITIES

As a real estate professional, you must look for opportunities to procure and grow your business as well as embrace and utilize the methods for conducting business. As I stated in the introduction, if you do not accept technology and utilize it, then you will not be successful in today's real estate marketplace. This section will focus on these points, how can you grow your business using the Internet and what web based practices must you understand to conduct business as a real estate professional using the Internet.

How Can I Grow My Business Using The Internet?

In discussing growing your business using the Internet, your focus should be to evaluate business that can actually be procured using the Internet. I have already discussed marketing yourself on your own website as well as through other sites like Trulia® or Facebook®; it's great to make yourself available to the public or through your website, and it should definitely be part of your marketing strategy, but how can you proactively procure business using the Internet? I will discuss three ways to procure business via the Internet. I will discuss social networking, corporate needs, and foreclosures. There are many other ways to proactively engage in practicing real estate through Internet leads, but hopefully these three areas will get you to start thinking in creative ways to procure business and develop a niche in the digital marketplace.

I discussed an entire section on social media in terms of describing and understanding it; however, with regard to procuring business, it can be a gold mine, especially with Facebook®. With the number of social media users being so high and the expansive nature of the posts that take place, daily monitoring of your network can yield business. Social media users openly discuss many personal decisions including moving or even the thought that moving or relocating may be on their horizon. First, make sure your network is aware that you are a licensed real estate professional, and second be proactive in reaching out to posts that suggest a move, and ask for their business. It is unfortunate, but statistics show that most sales professionals rarely directly ask for a potential clients business. If someone in your network is purchasing or leasing real estate, chances are they will be using a real estate professional, so why not you? Do not be shy or reactive; be proactive in asking for their business.

Many corporate property needs are openly displayed on their web sites in terms of specific geographic areas that they are actively engaged in procuring land and/or real estate space (either in terms of leases or purchases). You can monitor these websites to see if your market area is on a specific company's target. By knowing a ready, willing, and able buyer is present, you can search for an available property (or even property that may not be actively marketed through a brokerage agreement) and broker the transaction.

Foreclosures in the market place have turned digital. Most REO (real estate owned) property owners are using the Internet to market available properties. Many banks as well as government entities post property that it owns on the Internet. Many of these sites will allow you to sign up with them if you desire to list their properties and this is a viable business opportunity; however, there are also other opportunities. As you develop your network, you will develop relationships in your network that include investors whom desire to purchase property in order for rental income or to flip and procure a short term income. By monitoring sites such as local and national banks, homepath.com, the HUD Home Store, and other such sites, you will have your pulse on the foreclosure market and this will allow you to procure business.

Web Based Practices of Real Estate

Home Path®

As the real estate industry continues to journey deeper into the use of technology, many organizations are requiring the use of technology to conduct basic real estate activities. For example, some organizations that own real estate require that offers be submitted using the Internet and that all communication be in digital form (email, etc.). For example, I mentioned homepath.com in the previous paragraph. Home Path® is Fannie Mae's web site and in order to submit an offer on one of its properties, a real estate professional must submit the offer digitally through the web site. The properties on Home Path® are foreclosures and they are listed with local real estate brokers, but if you have a buyer who wants to make an offer on one of these properties, then it must be done through the web site. In traditional real estate practice, the selling agent submits the offer through the listing agent, but not on sites like Home Path®, the selling agent submits digitally straight to the seller. Real estate professionals must sign up at homepath.com; once the licensee is signed up, he or she can submit offers and review said offers.

hudhomestore.com

Another such site is the hudhomestore.com. This is the site used by the United States Department of Housing and Urban Development to sell properties that have been foreclosed on through the default of a FHA insured mortgages. These properties are listed through local real estate brokers, but once again as with homepath.com, offers for FHA foreclosures must be submitted through the hudhomestore.com. Real estate professionals with a sales license cannot individually register with this web site, the licensee's broker must first register or sponsored licensees cannot submit offers on behalf of clients. Before registering, a broker must apply for a NAID (Name Address Identifier) Number. It takes approximately two weeks for a broker to procure a NAID Number and once obtained, the broker may use the number to register with HUD. After a broker procures a NAID Number it is valid for a period of one year and the broker must recertify annually to keep the NAID Number active. If your broker is registered, then sales licensees and associate brokers may register; sales licensees and associate brokers will use the same NAID Number as their sponsoring broker. Please be cognizant of your broker's registration status, because if you have a client who wants to submit an offer on a property and your broker is not registered then you may lose out on the sale. Remember, registration takes a couple of weeks, and that period of time may prevent you from submitting an offer on a client's behalf if your broker is not already registered.

WEB TOOLS

There are many technological tools that can assist real estate professionals in the practice of real estate. All real estate professionals should be aware of these tools that are at their disposal which can assist in making the practice of real estate easier, more efficient, and ultimately more profitable. Because of the nature of the real estate industry, which is that of a primary need (especially in the residential market – people must have a place to live), the real estate industry has always been onerous with regard to documentation. However, with the progression of web based technology, digital tools are numerous, easy to use, and for the most part cost effective. In this section, I will discuss a few of these tools, please understand this is not an endorsement of these specific companies or products, but it is meant to be expressed as examples of products available in the industry to assist real estate professionals in the practice of real estate.

Web Sites

By now, everyone is familiar with web sites. A web site is a series of individual pages linked together using a domain name and stored on a web server. The web site or site can be used for many uses from advertising or supply information to providing intricate searches or databases inquiries, and in many cases the site can perform multiple functions. Web sites have become very affordable and easy to manage; there are many services that provide web site templates as well as develop packages, and with tools like Word Press, which is a free and open source content management system tool, a user can choose a template and develop their own site. Even if you aren't developing your own site, chances are the person or organization you are using for development purposes will probably use a tool such as Word Press.

Web sites are a necessity for all real estate professionals because outside of yourself, it is literally the number one advertisement for you as a real estate professional. The information on a web site will typically include information about you, your listings as well as other properties (local MLS listings can be linked through a real estate professional's web site to allow potential clients to view local listings from one source), community information, market data, and other extraneous information. For years, real estate professionals had to use expensive forms of marketing like print advertising to provide information about listings as well as to develop an individual brand in the marketplace, but with the use of tools like web sites, real estate professionals can now transmit endless amounts of information and data for a small fee. This is not meant to say that print advertising should not be used, it very well may be a form of marketing that you choose to use, but rather than paying for a larger expensive print advertisement or being limited to the amount of information that you can display, a web site is not limited. In fact, real estate professionals who utilize print advertisement as part of their marketing mix also include their web address in the print advertisement as a means to redirect the potential client to their web site. At that point, the real estate professional goes from limited information because of space limitations to unlimited information. Your web site should be the center of your marketing campaign, whether you are passing out a business card, promotional writing pen, or in the aforementioned print advertising example, your web site address should be publicized everywhere.

One of the most important things to remember regarding your web site is that it is an extension of you. If your web site is not aesthetically appealing, if the content is bad, if you have misspellings, or any such problems, then it may hurt your business. How can a client entrust you in assisting him/her with making the largest financial decision of their life, when your professional image is suspect. Please be cognizant of all aspects of your web site because you want it to be an asset and not a liability. Also, remember the Louisiana Real Estate Commission's Rules and Regulations have a specific set of guidelines that must be followed when advertising on the Internet.

Digital Agreement Services

Formulator®

Formulator® is a web based program that allows real estate professionals to write digital real estate agreements and it has an extensive library of real estate agreements that are specific to Louisiana. Real estate professionals can fill in the blanks to whatever agreements they need, save the documents online under their account and email them to their client in PDF format. This eliminates the need to hand write agreements, then fax or scan and then email them. The cost of Formulator® is very affordable, as of the writing of this course; the annual subscription fee is approximately \$100 per year. The company that creates Formulator® also has offline solutions and other products including DocuSign® integration. It is also important to state that although programs such as Formulator® are great tools for real estate professionals, the use of these programs cannot be misconstrued to be a substitute for the records retention requirements as set forth in the Louisiana Real Estate License Law. There are also other organizations that offer digital agreement services and some brokerage companies have proprietary digital agreement services

Digital Signature Services

DocuSign®

DocuSign® is a service that allows its users to utilize an esignature when signing documents. An esignature is when a party to an agreement signs a digital signature. The use of an esignature is as binding as a written signature. DocuSign® allows real estate professionals to upload documents for signing and the parties to the agreement can simply type their initials and/or name on the document. This service can be utilized on many mobile devices including but not limited to phones, tablet computers, personal computers, etc. and the service is very secure, which also makes it very appealing. Once the document(s) is signed, then it can be transmitted through electronic communication. The use of services such as DocuSign® allows the documentation process to remain in the digital realm without printing, signing, scanning, or faxing, which once again maximizes efficiency and productivity, thus increasing productivity. Like Formulator®, a real estate professional can purchase an annual subscription to DocuSign® and as of the writing of this course, the annual fee for this service starts at approximately \$180. Once again, there are other esignature services available in the marketplace, research them all in order to choose the one that best fits your individual needs.

Hybrid Services

Offer Xchange®

Another interesting tool available in the marketplace is Offer Xchange®. Offer Xchange® combines digital agreements and digital signatures into one service. This service provides the agreements, and then the parties to the agreement can securely login and digitally sign the agreement. The service even provides a status update, for example changing the status of the offer to “accepted”. Hybrid Services such as Offer Xchange® or services that can be integrated such as Formulator® and DocuSign® can save time and money for real estate professionals. As of the writing of this course, the fee for this service is \$29.95 per month.

Mobile Applications

There are many mobile applications (apps) that can be purchased on a smart phone and used as tools for practicing real estate. This section will discuss a few apps that are used in the real estate industry, but I would encourage real estate professionals to research all real estate related apps because this is not an exhaustive list but rather a means to have real estate professionals think in this direction and utilize apps that can assist in the daily practice of real estate. Also, there are apps that are added almost daily and new to the market; therefore, review the below available apps and think about how these and other apps can assist real estate professionals with their work.

JotNotPro®

JotNotPro® is a mobile phone application that can be used to scan documents. The goal is to keep documents in digital format but for the occasion that you have a hard copy and need to email or fax a document to someone, JotNotPro® is a simple and cost effective solution for on the go scanning. Once the app is purchased, the user can scan one or more pages and electronically communicate the document in PDF format. The document will also be saved in the app program. Hence, a real estate professional can have a hard copy of any agreement, have a client sign it, and then take a picture of the document through the app, process it, and then email or fax it to the client and/or cooperating real estate professional on the spot. The quality is serviceable and at the time of the writing of this course, the app is a one-time \$1.99 fee. As with the other tools in this section, there are competing brands and the real estate professionals should research them to find the best fit.

Mortgage Calculators

There are a variety of mortgage calculator applications that are available for a low cost and even some that are free. In the far majority of transactions in which the real estate professional is representing a buyer, the buyer will ask the amount of a monthly payment, and because mortgage loans are amortized, a program will be needed to calculate the payment. By using a mortgage calculator app, the real estate professional can very quickly answer this and other mortgage related questions.

CoreLogic Fusion

If a real estate professional is a member of their local multiple listing service, then the real estate professional can download this app and have mobile access to the MLS. Many licensees use I-Phone's and I-Pad's, which are Apple products and will not support the platform that local multiple listing services are built on, but with this app, real estate professionals can login and search the MLS with these products. By doing this, real estate professionals will have real time MLS searches and not lose precious time and valuable transactions by having to return to an Internet hot spot for searches. As of the writing of this course, this app is free, but the licensee must be a member of their local MLS to login to the system.

Google Maps

Google Maps can perform multiple actions that can assist with the day to day functions of real estate professionals. This app can provide voice guided navigation for directions to properties as well as visual views for around the properties. A client may ask what is beyond a wooded area behind a specific property; with Google Maps a real estate professional can answer that question. Google Maps also allows the user to save searches for future usage, and as of the writing of this course this app is free.

Trulia®, Zillow® and Realtor.com

I previously discussed Trulia®, Zillow®, and the realtor.com® web sites. These web sites have their own apps that can be downloaded to a mobile device. Real estate professionals and consumers alike can use the functionality of these web sites in an app format to assist with property searches, valuations, and other tools available with these sites. As of the time of the writing of this course, these apps are free.

CONCLUSION

The real estate industry is completely immersed in technology. There isn't a single facet of the industry that isn't excluded from technology, from marketing to property searches to market research to agreements, every aspect of the industry is technology based. Technology is no longer a luxury but now a necessity. If a person decides to enter the real estate industry as a licensed real estate professional and is not technology proficient or is not willing to become technology proficient, then the message is simple, chose a different profession because it is not feasible to practice real estate without using technology. Many real estate professionals are very familiar with the concepts, tools, and resources discussed herein, but I would encourage you to learn more because technology is progressing and changing at a rapid rate. As a real estate professional embrace the change, stay ahead of the curve, and never stop learning, this along with your hard work will be pivotal in your success as a licensed real estate professional.

ADVERTISING RULES AND REGULATIONS

LAWS AND RULES PART I

Introduction

The Louisiana Real Estate Commission is charged with protecting the public.

All of the advertising rules and regulations are meant to prevent confusion on the part of the public. These rules and laws are not meant to make the agents' lives easier but to ensure confidence in the public that all advertising made by licensees is true and accurate and in accordance with the laws and rules and regulations of the Louisiana Real Estate Commission.

A Good Week For...

Calling the boss a jerk, after the National Labor Relations Board ruled that workers can't be fired for complaining about their jobs on Facebook and other social-networking websites.

The USA, after an international poll by social-networking sites Badoo.com found that Americans are the world's "coolest nationality". Because of perceptions of widespread anti-Americanism, said a Badoo spokesman, "we sometimes forget how many people across the world consider Americans seriously cool".

The future of civilization, after London's Science Museum asked 3,000 adults to name what they couldn't live without. Facebook came in fifth, ahead of flushing toilets, showers, and fresh vegetables.

The Week, September 23, 2011

LSA – R. S. 37: 1455. Causes for censure, suspension, or revocation of license, registration, or certification

- A. The commission may censure a licensee, registrant, or certificate holder or conditionally or unconditionally suspend or revoke any license, registration, or certificate issued under this Chapter, levy fines or impose civil penalties not to exceed five thousand dollars, or impose continuing education requirements on licensees, registrants, or certificate holders if, in the opinion of the commission, a licensee, registrant, or certificate holder is performing or attempting to perform or has performed or has attempted to perform any of the following acts:
- (12) Offering real estate for sale or lease on terms other than those authorized by the owner or his authorized agent.
- (35) Using advertising that is misleading or inaccurate.

Use of MLS is Not Considered Advertising

Chapter 25. Advertising; Disclosures; Representations

§2501. Disclosures and Representations

- A. Agreements between brokers to allow property data to be shared and disseminated to clients, customers, or prospective clients, including but not limited to web-based or email multiple listing service property data, IDX or VOW property data does not constitute advertising or advertisement as to the property data shared.

Discussion:

- *Information listed with MLS is not considered advertising under the Rules & Regulations because this information should be accessible only through the broker's website where all the required information should appear.*
- *The Louisiana Real Estate Commission has received complaints alleging that a licensee has breached the "broker agreement" regarding how data is shared; however, this would not be within the jurisdiction of the Louisiana Real Estate Commission. Some Realtor Boards allow information to be printed and some do not. This is a Board issue.*

Advertising Must Be Under Direct Supervision of Broker

- B. All advertising for property listed by or services performed by a licensed individual real estate broker or a licensed corporation, limited liability company, or partnership, and any advertising for property listed by or services performed by a licensed individual real estate broker or a licensed corporation, limited liability company, or partnership by sponsored licensees or employees, shall be under the direct supervision of and approved by the licensed individual real estate broker or designated qualifying broker of the licensed corporation, limited liability company, or partnership.

Discussion:

- *Louisiana Real Estate Commission Staff Policy - Each licensee is responsible for compliance. The fine for a first offense is \$75, second offense is \$150, and for a third offense the qualifying broker will be charged and both must appear at a formal hearing before the Commissioners. The Louisiana Real Estate Commission will verify that the qualifying broker has procedures in place to supervise and approve agents' advertisements.*

Trade Names

- C. Any trade name used by a licensee, registrant or certificate holder in advertising shall be a trade name that is a clearly identifiable entity that will distinguish itself from other licensees, registrants or certificate holders.
- D. All advertising by a licensed salesperson, associate broker, individual real estate broker, or licensed corporation, limited liability company, or partnership shall include their business name, which for the purpose of these rules shall mean the name in which that salesperson, associate broker, individual real estate broker, or licensed corporation, limited liability company, or partnership is on record with the commission as doing business as a licensee of the commission or, in the case of a trade name, that which is registered with the Secretary of State and on record with the Commission.

Discussion:

- *If you open a real estate brokerage that has a name other than the name of the sponsoring broker, you must have a separate license and separate Errors and Omissions insurance for that brokerage.*
- *You must not abbreviate or omit - names should be exact. (Must include Inc., or LLC) unless company has registered a second trade name as in Baker & Co. rather than Baker and Company, etc.*
- *If you choose to use an abbreviated name, it must be registered as a trade name.*
 - *An "individual real estate broker" license can be issued in the name of the sponsoring broker and can have a trade name registered to that license. They are operating as a sole proprietorship with or without a trade name.*
 - *If they are operating as a separate corporation, LLC, partnership with a tax id number, they will have a trade name = PAPER ENTITY.*
 - *Each separate license (individual, associate broker, salesperson, and corporation) must carry its own Errors and Omissions insurance.*

Team Names

- E. A group or team name may be used in an advertisement only with the approval of the sponsoring broker. Any person listed as a group or team member in the advertisement must be a licensee sponsored by the sponsoring broker.

Discussion:

- *A group or team name being used must have the approval of the sponsoring broker.*
- *§1431: Definitions, "Real Estate Activity" (e): According to the license law you may not advertise that you are in the business of real estate without holding a valid real estate license. Therefore, members of a team who are not licensed by that particular sponsoring broker, or are unlicensed, cannot be in the advertisement.*

What's wrong with the ad?



- All members not licensed
- First and last names not listed
- Name of broker not listed
- Broker's phone number not listed

The chief investigator for the Louisiana Real Estate Commission suggests experience years be listed separately.

- Must use first and last name in ad
- Both members have to be licensed by same broker
- Cannot have team name that is confusing between team and brokerage company

F. In all advertising, the salesperson or associate broker must include the name and telephone number of the sponsoring broker. The broker's name and telephone number must be conspicuous, discernible, and easily recognized by the public.

Definintions

Advertising:

- The action of calling something to the attention of the public, especially by paid announcements
- A form of communication used to persuade an audience to take some action with respect to products, services, or ideas
- The activity of attracting public attention to a product or business, as by paid announcements in the print, broadcast, or electronic media
- Social network advertising is a term that is used to describe a form of online advertising that focuses on social networking sites. One of the major benefits of advertising on a social networking site is that advertisers can take advantage of the user's demographic information and target their ads appropriately.

Discernible:

- Perceptible, as by the faculty of vision or intellect
- Able to be detected by the eyes or other senses

The philosophy of the Commission and the measuring stick they will use in enforcing the rule requiring wording be discernible, is that they want and are interested in being able to see the broker's name and telephone number as easily as the agent's name and telephone number.

Conspicuous:

- Easy to notice
- Obvious
- Attracting attention

Discussion:

- *The broker's name and telephone number must be discernible. Even though it doesn't specify "telephone number" under "Internet Advertising, §2501-F", make it clear that the phone number should be there.*
- *Direct lines and phone numbers owned by the brokerage company that by-pass the brokerage's main line and go directly to the agent are considered to violate the spirit of the Rule. What the Commission wants is for the public to be able to call the telephone number in the ad and get in touch with the broker or branch supervisor if they so desire.*

What's wrong with this name?

The full name "Century 21 Stafford's Extraordinary Group" should be conspicuous, discernable, and easily identifiable by the public. This is called "disappearing ink" by the investigators at the Louisiana Real Estate Commission.

QUESTION and ANSWER

Q. When representing my brokerage's name, do we need the broker's telephone number on the sign placed on our office?

A. No, an office sign is not considered to be an advertisement. It is considered to be a "locator".

G. *If allowed by the sponsoring broker, the salesperson or associate broker may include in the advertisement:*

- 1. The salesperson's or associate broker's personal logo or insignia, which cannot be construed as that of a company name, and which must include the name and telephone number of the sponsoring broker;*
- 2. The salesperson's or associate broker's contact information;*
- 3. A group or team name, as long as the name(s) of the salesperson(s) and/or associate broker(s) are included near the team reference and cannot be construed as that of a company name; and*
- 4. A slogan that may not be construed as that of a company name.*

Discussion:

- *One of many reasons for this rule, other than not to confuse the public, is to prohibit a team from appearing to be a brokerage company.*

Advertising and the Brokerage

Real estate advertising typically falls into one of two main categories:

1. The first category includes advertising the services offered by the licensee. The purpose is to draw the attention of potential clients to these services and not to a specific property for sale or lease. Examples of this type of advertising are those television or radio ads extolling the merits of a licensee or a brokerage.
2. The second category concerns brokerage transactions and includes advertising real estate. This type of advertising is done in newspapers and trade publications, on specialized television networks, on listing-cut sheets, and on the Web. The purpose is to advertise one or more properties for sale or lease.

To advertise brokerage transactions, the Louisiana Rules and Regulations require brokers and salespeople to have the seller's or lessor's written permission to advertise the property. In practice, this means that a licensee can advertise a property for sale or lease only if they have a brokerage contract authorizing them to do so.

Caution must be used when a listing brokerage authorizes another brokerage or salesperson to advertise a property. If you want to advertise another brokerage's listing, you must obtain the permission of the owner and the listing broker.

One way to ensure whose listings are whose is to create two links for listings, one titled "My Listings" and one titled "Other listings" with each link taking you to a separate and correspondingly titled Web page.

When advertising completed transactions make sure your information is not misleading or false in nature.

Suggestions for Good Advertising

- Create relevant and specific ads
- Target the right audience
- Set a daily advertising budget
- Keep it short and simple
- Keep it engaging
- Include a call to action

Keep Information on Web Sites Current

Make sure not only your name and number, but your broker's name and number, are on all forms of communication and on every webpage.

The Broker Is Ultimately Responsible!

Brokers must take all reasonable means to make sure that the licensees they sponsor comply with the provisions of the Louisiana Real Estate License Law and Commission Rules and Regulations. Brokers must therefore ensure that their own advertising, and any advertising done on their behalf by their salespeople, is consistent with the rules.

Business Names

A broker selecting a brokerage name must keep a few practical aspects in mind.

The Commission recommends that you choose a name that is not too long, because under the Louisiana Real Estate Commission Rules, all advertising must include the full name of the brokerage as it appears on the brokerage license.

The broker and their salespeople must include the brokerage name in all advertising and cannot use a short form even if, under certain circumstances, it would seem desirable to do so.

Names on Licenses

The Louisiana Real Estate Commission will be taking a hard look at licensee advertising, so please act promptly to resolve any issues related to the name that you use in your advertising and marketing campaigns, or any other real estate license activity. Below are some of the more frequently asked questions regarding names on licenses:

QUESTIONS and ANSWERS

- Q:** My registered legal name on my real estate license is Arnett Bob Brown. Must I use my middle name in real estate advertisement
- A:** No, you do not have to use your middle name, but you must use first and last name unless you have a filed a DBA with the Commission to use Bob Brown. Then I would be able to use either Arnett Brown, Arnett Bob Brown, or Bob Brown.
- Q:** My legal name is John Jacob Doe, but I am known as "Jack" to my friends, family and business clients. What must I do to be in compliance when advertising?
- A:** Your legal name must be registered with the Commission, as well as your DBA/Nick Name, Jack Doe. You may advertise as John Doe, John Jacob Doe, or Jack Doe. You are not required to use your middle name in advertisements, but your last name must always be included.
- Q:** My legal name is Mary Alice Smith, but I am known by my middle name, Alice, to friends, family and business clients. My legal name is registered with the commission, but I want to advertise as Alice Smith. What must I do to be in compliance when advertising?
- A:** You should register Alice Smith as a DBA/Nick Name.

LAWS AND RULES PART II

§2503. Owner Authorization

- A. No broker or licensee sponsored by said broker shall in any way advertise property belonging to other persons as being for sale or rent or place a sign on any such property offering the property for sale or rent without first obtaining the written authorization to do so by all owners of the property or their authorized attorney in fact.

Discussion:

- “Attorney in fact” means the person holding power of attorney. This is often used when family members or multiple persons own the property. It is much easier for the licensee to obtain signatures on documents when dealing with just one person who holds a power of attorney for the other family members. §2503 is also an area in which the licensee should have a basic knowledge of inheritance laws.
- An executrix or executor cannot sign a contract on behalf of the heirs unless they have a power of attorney. The Louisiana Real Estate Commission has received complaints about these parties signing the listing agreement instead of the rightful heirs.

Inheritance Laws in Louisiana

Louisiana, being the only Civil Law state in the union, and only forced heirship state, is unique in its inheritance laws which strive to be fair and equitable to both the surviving spouse and the children of the deceased. Complete and perfect ownership includes three sticks in the bundle of rights:

1. Abusus (title to the property)
2. Usus (the use of the property)
3. Fructus (the fruits or revenue from the property)

Community property is what is owned by the marriage. Separate property is what you owned prior to marriage and/or things acquired during the marriage, but not by the marriage, for example, inherited property. Keep in mind that even though you acquired something prior to marriage, but you paid for some or all of it out of community funds, it could make it whole or partially community property. For example, if you bought a house two months before marriage, but paid the house note out of community funds or a joint checking account, the house may now be community property. Remember, it only takes one signature to acquire community property, but it takes two signatures to sell it.

The Louisiana Real Estate Commission has received complaints concerning a listing agent who allowed an “almost” ex-husband to sign as sole owner on the listing and purchase agreements on a community property home. The divorce was not final, but the ex-husband told the licensee that he was the only owner of the property. When the wife called the licensee to complain, the licensee did not remove the listing from his website or from MLS.

Community Property

If Mr. Brown should die today intestate (with no will), and is survived by his wife and three children, his half of the community property would go to his three children. His widow would retain her half of the community property. The children would receive abusus or the title to their half of the property, with the state of Louisiana giving usus and fructus to the surviving spouse until death or remarriage. If you combine the words usus and fructus, we now have a new word “usufruct” which is a personal servitude over the half of the property belonging to the children. Upon listing this house you would need to account for four signatures - the widow and the three children because there are four owners of this house.

The separate property owned by the deceased Mr. Brown would go to his three children, and they would have abusus, usus, and fructus of this property. The widow would have no interest in the separate property as Mr. Brown died intestate.

If Mr. Brown died testate, the signatures needed would depend upon the ages of his children and/or what is stated in the will. If your child is no longer 23 years of age or younger, then he or she is not a forced heir and does not have to be included in the will, unless the child is physically or mentally handicapped. If handicapped, there is no age restriction.

Forced Portion or Legitime:

The forced portion of the property of the decedent is the portion that his forced heirs must receive upon his death. The balance of the decedent's estate is called the disposable portion.

Disposable Portion:

The disposable portion is three-fourths if the decedent leaves one heir at his death and one-half if the decedent leaves two or more forced heirs.

Forced Heirs:

Forced heirs are the children of the decedent who at the time of the death of the decedent are:

- 23 years of age or younger
- Any age, but because of some mental incapacity or physical infirmity are permanently incapable of taking care of their persons or managing their property

Disinherison:

There are specific reasons for which a parent may disinherit a forced heir but they are seldom used.

When it comes to record of title, the real estate agent can rely upon what is told to him or her by the so-called owner, but in cases of death or divorce, the agent should be prompted to inquire further as to legal ownership. Searching the courthouse records has been ruled by some courts as being out of the area of expertise for licensees, but death, separation, or divorce should raise red flags and invite inquiry. Divorce does not always include a property settlement.

Remember, if the couple is separated, signatures of both husband and wife must be on the listing agreement unless one holds a power of attorney for the other.

Remember, the law does not make an exception just because the property is owned by several family members some of whom are out of state making it difficult for the licensee to obtain their signatures.

- B. *Undivided real estate may be offered for sale or lease with the written consent of the owner of the property to be sold or leased as to his undivided portion of the property.*

Discussion:

- This has not always been the case. Just in the last few years this rule was added to stipulate that partial interest owners could sell their interest without involving the other owners. The percentage being sold should be stated in the advertisement; however, this is not specifically required in the laws or rules.
 - **The law: 37:1455.A. (11):** Undivided real estate may be offered for sale or lease with the written consent of the owner of the property to be sold or leased as to his undivided portion of the property.
 - **The rule: 2503:B.** Undivided real estate may be offered for sale or lease with the written consent of the owner of the property to be sold or leased as to his undivided portion of the property.

Truth in Advertising

False/Deceptive Advertising

False advertising or deceptive advertising is the use of false or misleading statements in advertising. As advertising has the potential to persuade people into commercial transactions that they might otherwise avoid, many governments around the world use regulations to control false, deceptive or misleading advertising.

Truth

Truth refers to essentially the same concept, that customers have the right to know what they are buying, and that all necessary information should be on the label.

Advertising

Advertising plays a key role in the real estate industry because it influences the purchasing decisions of the consumer. Truthful advertising benefits the consumer and enhances the image of the industry.

Conversely, misleading advertising can negatively affect consumers, licensee's business and the integrity of the real estate industry.

§2505. Accuracy in Advertising

- A. All advertising shall be an accurate representation of the property advertised. No broker or licensee sponsored by said broker shall use advertising which is misleading or inaccurate or in any way misrepresents any property, terms, value, policies, or services of the business conducted. The advertising shall not include any name or trade name of any franchiser or real estate organization or association of which the licensee is not a member or franchisee.

Discussion:

- The most common type of violation with real estate organizations or associations is claiming to be a **REALTOR®** when in fact they are not, or using the trademark R symbol. The acronym "TLC" sometimes is used in its broadest sense.

Other Common Errors:

- Listing total square footage as "living area" is misleading.
- Confusing arpent with acre is also misleading; 100 arpents equals about 85 acres. Arpent is NOT French for acre. An arpent is 192 ft. X 192 ft. An acre is 208.71 ft. X 208.71 ft.
- We have agents representing themselves using a team or group name although they have no team members! That would be misleading and inaccurate.
- Advertisements using only the first name.
- If a firm is affiliated with a franchise organization, all advertisements must disclose to the public that the firm is "independently owned and operated".
- Advertising "new air conditioner" when only the compressor has been replaced, not the coils, or vice versa.
- Advertising property as waterfront when there is a small man-made pond in the front yard.
- Advertising as a team but only the team leader is pictured and other team members are not listed or named. If you do not include team members you cannot advertise as a team.
- Advertising a water treatment as a pond. This actually happened according to the investigative staff, but the true nature was revealed in the summer after the sale.

QUESTION and ANSWER

- Q.** My signs do not include the disclosure that our office is "Independently Owned and Operated". How can I get into compliance?
- A.** You can amend your current signs using stickers with the printed required disclosure.

§2507. Advertisements of Residential Property

All printed advertisements for the sale or lease of residential real estate shall indicate the month and year the advertisement is printed, published, or distributed. Advertisements printed or published in newspapers, real estate trade publications and commercial magazines and brochures bearing an issue or publication date will be considered in compliance with this Section.

Discussion:

- Flyers placed in a box by the “for sale” sign offering information about the listed property should also be dated with month and year that it was printed, published, or distributed. The reason advertising needs to be dated is to insure that the ad is in compliance with rules and regulations in effect at that time and to allow the public to know how old the information is. This includes flyers at open houses and/or “choose your neighbor” flyers and post cards.

QUESTION and ANSWER

- Q.** Is there a requirement to place the current date on printed flyers?
- A.** Dates are not required on newspapers, sales magazines, or other publications bearing issue number as these publications already include the date or volume number.

Franchises: You Ought to Know

§2509. Advertisements by Franchise Organizations

Any licensed broker or salesperson affiliated with a franchise organization must disclose to the public that the real estate brokerage firm is independently owned and operated in all advertising and on every page of the website.

The chief investigator for the Louisiana Real Estate Commission recommends that this information be included on the first or last page in all electronic communication.

It is recommended that the information be on the signature page which is the last page.

Discussion Question

Sally Salesperson is an agent for Western Realty, a franchise company mainly in the western United States licensed to do business in Louisiana, ran an ad in the newspaper featuring her highest priced listing.

Which of the following **MUST** be in the ad?

1	Broker's name	Yes	No
2	Broker's telephone number	Yes	No
3	Broker's street address	Yes	No
4	Sally Salesperson's name	Yes	No
5	Sally Salesperson's telephone number	Yes	No
6	Each office is independently owned and operated	Yes	No
7	This property is O/A	Yes	No
8	Price of property	Yes	No
9	Picture of property	Yes	No
10	Address of property	Yes	No

Answers:

Yes – 1,2,and 6;

No – 3,4,5,7,8,9,and 10

What is missing from the ad?



- Independently owned and operated
- No company telephone number
- No company name

Flyer in Yard Box:

18747 Wildlife Way Ct.
\$ 307,000



4 Bedrooms/2.5 Baths
2,385 sq ft living area

For more information visit:
www.18747WildlifeWay.com

- Don't Miss Out on this Beauty
- Beautiful Lake at White Oak
- Gunite Pool w/large backyard
- Two Oak Trees on Property
- Lot size is 90x201x124x193
- Large Den Area
- Kitchen has open breakfast area
- Real Wood Burning Fireplace
- Many Updates!!
- \$3000 Flooring Allowance

Sally Salesperson
Cell: 225-500-5003
Office: 225-600-1000
sally@FNRE.com
www.FNRE.com



FIRST NATIONAL
REAL ESTATE
FRANCHISE CO.

Information herein is furnished by the seller to the best of his knowledge, and is subject to verification by the purchaser. One agent assumes no liability for errors, omissions, price changes, prior sale or without sale without notice. In accordance with the law, this property is offered without regard to race, color, religion, sex, handicap, age, marital status or national origin. Minimum investment \$25,000. 2/1/03

What is missing from this ad?

- No date (month and year) printed, published or distributed
- Doesn't say "independently owned and operated"

License Status; Internet Advertising; Team Advertising

§2511. Agent Owner-Licensed Agent

- A. A licensed broker or salesperson who offers property in which he or she owns any interest as being for sale or rent shall state in any advertising, and on any sign placed on the property, that he or she is a licensed real estate agent.
- B. Any licensed broker or salesperson that advertises, or offers to purchase or rent property for his or her own full or partial interest shall state in any advertisement that he or she is a licensed real estate agent.
- C. Including the term "licensed real estate agent" in any advertisement or on any sign shall be sufficient to satisfy this requirement.
- D. This Section is not applicable to the sale, rental, or acquisition of property by licensees under a contractual agreement with a licensed Louisiana real estate broker.

Discussion:

- The term "owner agent" is the most common way to disclose this even though the rule uses the term "licensed real estate agent". However, disclosure does not stop there: remember you must include in the lease and/or buy-sell agreement that you are a licensed real estate agent. That applies to an agent who is either a buyer or seller, lessor or lessee. It also applies when your license is inactive. Just because you have an inactive license doesn't mean you're exempt from knowledge of the rules. Your knowledge is not inactive!
- The executive director, Bruce Unangst of the Louisiana Real Estate Commission has ruled that the term "owner agent" is acceptable, but "O/A" is not.
- If you list your own property or use your real estate license to buy property through your broker, the term "owner agent" does not have to appear in any advertisements, but your broker's name and telephone number must be in the ad. It doesn't hurt to put "owner agent" on real estate company signs for listed property, but it is not required.
- If you act as a "for sale by owner" or lessor, lessee, or purchaser, you must include "licensed real estate agent" in the contract even if you are using a broker. You must also include the sexual predator website if the transaction involves residential property (4 plex or less).
- Remember, separate from advertising disclosure of owner/agent, you must disclose in writing that you are a licensee before entering into any real estate contract as a seller/buyer, lessee/lessor. Even if the principal has knowledge of your vocation ---you must put it in writing.

Discussion Question:

Broker Bob, a licensed real estate broker, ran an ad for a ranch he owns in "Ranches for the Rich, Edition XXVII". He did not list the ranch with his company and elected to be a "for sale by owner".

Which of the following must be in the ad?

1	Date the ad was published or distributed	Yes	No
2	Broker's license number	Yes	No
3	Broker's name	Yes	No
4	Broker's telephone number	Yes	No
5	O/Agent	Yes	No
6	Address of brokerage office	Yes	No
7	Country in which main office is located	Yes	No
8	Owner/Agent	Yes	No

Answers:

Yes – 8;

No – 1,2,3,4,5,6, and 7

Advertising Without a Valid License

License Status and Advertising

What happens with advertisements following cancellation, abandonment, expiration or suspension of a licensee's license?

Whether a suspension is voluntary or imposed, a licensee must cease all advertising. Advertising is considered trading in real estate and therefore, cannot be performed by any licensee without a valid license for someone other than advertising their own real estate.

A licensee who does not hold a valid license must:

- Cease all advertising in periodicals
- Cease all soliciting of clients by mail, e-mail or phone
- Remove any advertising sign or other advertisement
- Remove all road signs
- Cease all advertising on Web sites and Internet classifieds
- Notify local REALTOR® boards of which the person is a member, and remove any listing on MLS, and the broker must appoint a replacement
- Remove all billboards on thoroughfares and highways
- Remove all ads on company or personal vehicles
- Remove all signs on buses, public benches, in arenas or other public places.

This also applies to inactive licensees except when acting as a for sale by owner and not as a licensee, however on all advertising the inactive licensee must disclose that he is a licensee in buying, selling, leasing, and renting and must disclose that he is a licensed real estate agent in all Buy-Sell agreements and Lease Agreements, whether lessee or lessor.

§2515. Internet Advertising

A. A real estate broker advertising or marketing on a site on the Internet must include the following data on each page of the site on which the advertisement appears:

1. the broker's name or trade name as registered with the commission;
2. the city and state in which the broker's main office or branch office is located.

Discussion:

Under the new rules, the jurisdiction in which you are licensed, as well as country, are no longer required.

Even though it does not say "telephone number has to be included" in §2515, after discussion with the Louisiana Real Estate Commission, they are of the firm opinion that the telephone number must be included in all advertising as so stated in §2501-F: *"in all advertising the salesperson or associate broker must include the name and telephone number of the sponsoring broker". The broker's name and telephone number must be conspicuous, discernible and easily identifiable by the public.*

B. A real estate broker using any Internet electronic communication for advertising or marketing, including but not limited to, e-mail, email discussion groups, and bulletin boards, must include the following data on the first or last page of all communications:

1. the broker's name or trade name as registered with the commission;
2. the city and state in which the broker's main office or branch office is located.

Discussion:

- Again, country has been eliminated as a requirement.
- This rule does not apply to websites but to electronic communication, so the requirement is either first or last page of all communications.

QUESTION and ANSWER

Q. What is required on websites such as www.realtor.com

- A.** The Louisiana Real Estate Commission does not have jurisdiction over data shared via IDX, and there is no violation if you have no control over the site. However, if “enhancements” or promotional packages are purchased from realtor.com, Truila, or Zillow, all information must be included to avoid being charged with a violation.
- C. An associate broker or salesperson advertising or marketing on a site on the Internet must include the following data on each page of the site on which the licensee's advertisement or information appears:
1. the associate broker's or salesperson's name;
 2. the name or trade name of the licensed broker or agency listed on the license of the salesperson or associate broker;
 3. the city and state in which the broker's main office or branch office is located.

Discussion:

- This requirement is the same as that for brokers except that you must remember to always include the broker's name or trade name as listed on your license. This information has to appear on each page of the site.
- D. An associate broker or salesperson using any Internet electronic communication for advertising or marketing, included but not limited to, e-mail, email discussion groups, and bulletin boards, must include the following data on the first or last page of all communications:
1. the associate broker's or salesperson's name
 2. the name or trade name of the licensed broker or agency listed on the license of the salesperson or associate broker
 3. the city and state in which the broker's main office or branch office is located

Suggestion:

Include all information on signature page, including team name and first and last name of each team member, as per the chief investigator of the Louisiana Real Estate Commission.

Discussion:

- This requirement is also the same as for brokers except that the broker's name or trade name must appear as listed on your license. This information has to appear on the first or last page.

To Summarize

The following information must appear on first or last page for emails, and every page for Internet advertising:

- Name and telephone number of the brokerage firm
- City and state where office is located
- “Independently owned and operated” (if a franchise)
- If a team name is represented, it must include the first and last name of each team member
- All individuals who are listed as part of the team must be licensed and sponsored by that broker.
- Team names cannot be construed as that of a company name
- If names are included, first and last names must appear

Discussion Questions:

1. Sally Salesperson created her very own website. The new website must contain which of the following?
 - a. Broker's name, city, state, and phone number on first or last page
 - b. Broker's name, city, state, and phone number on each page
 - c. The term USA in the address
 - d. Sally's name and phone number must be on each page.
 - e. Since it's Sally's own website she doesn't need her broker's name on her website.

Answer: b

2. Sally salesperson sent an email to her very best client showing a picture of a listing Sally has that she thought her client would be interested in. Which of the following is TRUE?
 - a. The Broker's name, address and telephone number must be on each page.
 - b. The Broker's name, address and telephone number must be on the first or last page.
 - c. I don't care; I have an extra \$75 to give the LREC.
 - d. Either B or C is correct.

Answer: b

Team Advertising

Within a brokerage office, several licensees may get together and form a team. Similarly, husbands and wives, or parents and grown children, or business partners may get together and form a team. These teams can advertise themselves as such; there must not be any confusion between the team name and the employing brokerage.

In any advertising, the broker's name and telephone number must be included.

In an ad featuring a team photo, each person must be identified by their first and last names.

- Use of first names only is not acceptable.
- Last name only is not acceptable.
- Use of middle and last name is not acceptable unless registered with Louisiana Real Estate Commission as DBA ("doing business as"). This form is available within the "resources" area of this lesson.
- As with all advertising, you cannot make comparative claims without providing all the required elements for comparative claims.
- If you wish to use years of experience you should include each person's years of experience separately. This is a suggestion, not a rule.

Discussion:

- Although all advertising must be under the "direct supervision of the sponsoring broker", licensees are responsible for complying with the rules and regulations.
- The salesperson or associate broker will be charged if their advertisement fails to comply. Each person on a team will receive a separate citation if the team's advertisement is in violation of the rules.

QUESTION and ANSWER

- Q.** Can I promote myself or my team on one side of a business card as long as all required information is on the other side of the card?
- A.** This is acceptable as long as the brokerage's name and telephone number are conspicuous, easily identifiable, and discernable.

Cite & Fine: A Heads Up

The Louisiana Real Estate Commission's new Cite & Fine system, created to alleviate lengthy disciplinary procedures for common violations, is entering the final phase of development and was implemented October 20, 2011. It functions much like a traffic ticket. Violators will be provided a form in which they may elect to either pay the fine or attend a hearing to plead their case.

If a licensee attends a Cite & Fine hearing and is found guilty of the said violation, the licensee's name will be posted in the newsletter and on the website. The system was originally developed to help deal with advertising violations, but it has turned into a promising tool to assist in expediting other common real estate violations as well.

Licensees should review the Advertising Guidelines Checklist provided on the Louisiana Real Estate Commission website to ensure all advertisements are in compliance with the laws and rules.

Activities and Fines

LSA-R.S.37	ACTIVITY	FINE
1442.A	Conducting authorized activity after expiration of license.	\$325
1447	Failure to obtain required continuing or post-licensing education.	\$325
1449.1	Failure to use mandated purchase agreement.	\$75
1449.A, B	Failure to provide all parties to transaction with completed document within 5 days.	\$75
1449.D	Failure to maintain records for 5 years.	\$150
1455.A.(9)	Failure to disclose license status when acting as a principal.	\$150
1455.A.(21)	Failure to provide parties with an agency disclosure pamphlet or dual agency form.	\$75
1455.A.(33)	Failure to provide written property disclosure form.	\$75
RULES & REGULATIONS	ACTIVITY	FINE
Chapter 25	Improper advertising by licensee.	\$75
Chapter 27	Improper name of account, no signature for broker, escrow accounts interest bearing.	\$75
Chapter 29	Failure to disburse a deposit within 90 days of the broker having knowledge that a dispute exists.	\$250
Chapter 31	Failure to report change of address or telephone number.	\$75
Chapter 35	Failure to disclose status as a licensee.	\$75
Chapter 39	Failure to annotate.	\$75

Enforcement

- Upon receipt of a copy or photograph of advertisement, it will be reviewed utilizing established criteria to determine that a violation has occurred.
- A citation will be sent by certified mail to the licensee and to their sponsoring broker. The licensee will be directed to appear at the Commission for a scheduled Citation Review Hearing.
- If the licensee desires to admit to the violation and pay a \$75 fine within 30 days, the matter may be resolved informally.
- Failure to pay the fine within 30 days will result in the Executive Director issuing a Cease and Desist Order prohibiting any real estate activity.
- If the licensee has a second advertising violation, the fine will double. If there would be a third offense, they would be brought before the Commission for a formal hearing.

Promotional Advertising

Advertising vs. Promotions or Promotional Products

Caps, shirts, name tags, pens, calendars, magnetic signs of football schedules that go on refrigerators, coffee cups, etc. are considered promotions. However, that does not mean that a salesperson or associate broker may advertise just in their name only without providing the broker's name, but they can omit "independently owned and operated". Until this can be addressed further by the Commission, no citations will be issued in this area.

Home Inspections

BACKGROUND INFORMATION

Home inspections have become an integral part of real estate transactions, with the majority of homes sold in today's market undergoing the process. However, this has not always been the case.

When the home inspection profession first appeared on the real estate scene, it was not embraced with open arms by the real estate profession. Perhaps there was a feeling of vulnerability associated with the potential impact that a home inspection could have on a real estate transaction. Whatever the reason, it did not take long for the real estate industry to recognize the value of a home inspection in helping to shield brokers and agents from potential litigation. If there was ever any doubt about it, the **Easton v. Strassberger** court decision (199 Cal. Rptr. 383 (Cal.App. 1 Dist. 1984)) made it crystal clear.

Facts of the Case

Easton v. Strassburger was a 1984 California Appellate Court decision that expanded both the duty of real estate agents and the grounds for negligence in selling faulty residential property. The state Supreme Court declined to hear the case, giving it the force of law in the state.

Strassburger employed the firm of Valley of California as broker for the sale of their property. Easton purchased the property for \$170,000 in May 1976. One of the agents observed that the floor of a guest house was uneven, an indication of soil problems. There was also a net installed to repair damage from a slide which occurred just prior to the sale. The 1976 slide damaged the property so severely that the property was estimated to be worth \$20,000 in its damaged condition. There were two other slides in 1973 and 1975 which caused portions of the land to sink significantly. However, Strassburger never ordered a soil study and did not disclose these facts to Easton. Shortly after the sale, landslides again caused significant damage to the property. The slides occurred because a portion of the property was built on fill that was not properly engineered or compacted. The driveway was destroyed, walls cracked, and floors and doors warped.

Easton sued for fraudulent concealment and intentional and negligent misrepresentation. Easton filed suit against the Strassburgers, the contractors, the real estate agents, and three other parties. The trial court found all of the defendants negligent and awarded Easton \$197,000.

The appeal filed by the real estate agents is the basis of the case. The appellate court upheld the decision against the selling agents despite the fact that they had been equally deceived by the Strassburgers. The court held that agents, as licensed professionals, have a duty to not only disclose what they know, but also what they should know as professionals making “reasonable use” of their knowledge, skills, and experience.

A real estate agent owes a duty of care to other parties to a real estate transaction, even if he or she has not undertaken to act as their agent. Easton v. Strassburger, supra, held that a seller's agent has a duty to exercise care to discover and disclose to a prospective buyer of residential property any physical conditions and defects that might materially affect the value or desirability.

Easton v. Strassberger
(199 Cal. Rptr. 383 (Cal.App. 1 Dist. 1984))

In the eyes of the court, the agents saw and ignored “red flags” such as the mere presence of fill, uneven floors, and erosion netting that was placed on slopes. These things should have alerted them, as experienced real estate professionals, to potential problems. The court held that real estate agents have an affirmative duty to further investigate such obvious signs of distress.

Easton v. Strassburger is a landmark case that established a selling agent’s duty of inspection and disclosure to prospective purchasers. (The court limited its holding to residential property, expressing “no opinion” whether an agent’s obligation to conduct an inspection for defects for the buyer’s benefit applies to the sale of commercial real estate.)

And so, the wheels were placed in motion. Before 1985, there were no state regulations for home inspectors or home inspections, but today that has changed. Texas was the first state to enact legislation, but it was the Louisiana regulatory program that ranked number one in the American Society of Home Inspectors’ (ASHI) top five best states for home inspection (2008). States were graded according to the weight ASHI placed on regulation standards and were evaluated against criteria such as experience, education, testing requirements, standards of practice, and code of ethics.

LOUISIANA LAW AND RULES AND REGULATIONS

Basic Purpose

In 1999, with the enactment of **R.S. 37:1471 et seq.**, otherwise known as the **Louisiana Home Inspectors Licensing Law**, the Louisiana Legislature declared it in the best interest of the citizens of the state to require the licensing and regulation of home inspectors. The stated purpose of the law is to require qualifying criteria in a professional field in which unqualified individuals may injure or mislead the public and to contribute to the safety, health, and welfare of the people of this state.

Administration and Regulation

As provided in the law, the Louisiana home inspection industry is regulated by the **Louisiana State Board of Home Inspectors**, a seven-member panel whose duties and responsibilities are structured similar to those of the Louisiana Real Estate Commission:

Powers and Duties of the Board (R.S. 37:1475)

The law provides that the board shall:

- (1) Elect a chairman and a vice chairman, each to serve a term of one year, who may be reelected for subsequent terms.
- (2) Employ a secretary-treasurer who shall serve as the chief operating officer of the board, who shall serve at the pleasure of the board, and who shall employ such other staff as approved by the board.

- (3) Hold quarterly meetings each year, provided special meetings may be held at such time and place as specified or called by the chairman. The secretary-treasurer shall provide written notice of all meetings to the members of the board and to the interested public.
- (4) Adopt rules and regulations, in accordance with the Administrative Procedure Act, as the board deems necessary to administer and implement the provisions of this Chapter or to govern the practice of home inspectors in the state.
- (5) Issue, suspend, modify, or revoke licenses to practice as a home inspector in the state.
- (6) Report to the attorney general all persons who violate the provisions of this Chapter.
- (7) Maintain an up-to-date list of licensed home inspectors.
- (8) Adopt and approve a licensing examination, which may be administered by a nationally accepted testing service as determined by the board.
- (9) Adopt an official seal.
- (10) Adopt minimum standards of practice for home inspectors.
- (11) Have the authority to impose fines.
- (12) Adopt rules and regulations governing the manner and conditions under which credit shall be given by the board for participation in continuing professional education as the board may consider necessary.
- (13) Authorize any affidavit necessary for the issuance of any injunction or other legal process authorized under this Chapter or under the rules and regulations of the board.
- (14) Issue subpoenas to require attendance and testimony or the production of documents for the purpose of enforcing the provisions of this Chapter and the rules and regulations adopted pursuant to this Chapter and securing evidence of violations.
- (15) Have the authority to incur debt.

See Acts 1999, No. 61, §2; Acts 2003, No. 568, §1.

Definition of a Home Inspection and Other Relevant Terms (R.S. 37:1473.4-8)

A home inspection is a thorough non-destructive examination of the current condition of a home. It is **not** an appraisal (which determines market value) or a municipal inspection (which verifies local code compliance). A home inspector, therefore, will not "pass" or "fail" a house, but will accurately and objectively describe its physical condition and indicate potential problems or concerns.

To ensure that a home inspector provides an inspection service that complies with board standards, the law contains specific language that defines a home inspection and other relevant terms. As a real estate licensee, it could be helpful to become familiar with the definitions shown in the following excerpt from the Louisiana Home Inspectors Licensing Law:

"As used in this Chapter, the following words shall have the following meanings unless the context clearly indicates otherwise:

- (4) "Home inspection" means a written evaluation of two or more of the following component systems of a resale residential building:
 - (a) Electrical system
 - (b) Exterior system
 - (c) Insulation/ventilation system
 - (d) Heating and cooling systems
 - (e) Plumbing system
 - (f) Roofing system
 - (g) Structural system

- (h) Appliance system
 - (i) Interior system
 - (j) Any other related residential housing system as defined in the standards of practice prescribed by the board.
- (5) "Home inspector" means any person who, in accordance with the provisions of this Chapter, holds himself out as a home inspector to the general public or engages in the business of performing home inspections on resale residential buildings for compensation or who examines any component of a building, through visual means and through normal user controls, without the use of mathematical sciences.
 - (6) "Licensee" means any person who has been issued a license by the board in accordance with the provisions of this Chapter.
 - (7) "Residential resale building" means a structure intended to be or that is used as a residence and consists of four or less living units, excluding commercial use space or units, and is not for sale for the first time.
 - (8) "System" means a combination of interactive or interdependent components assembled to carry out one or more functions."

Acts 1999, No. 61, §2; Acts 2003, No. 568, §1.

General Exclusions

There are certain items that may not be found in a home inspection report. The significance of knowing these exclusions is the benefit they may provide in explaining the home inspection process to your client. In addition to what a buyer or seller can expect from a home inspection report, it is equally important to know what not to expect. Louisiana home inspectors **are not required** to inspect or report on:

- Life expectancy of any component or system;
- Causes of any condition or deficiency;
- Methods, materials, and costs of corrections;
- Suitability of the property for any specialized use;
- Compliance or non-compliance with codes, ordinances, statutes, regulatory requirements, special utility, insurance or restrictions;
- Any component or system that was not inspected and so stated in the home inspection report or pre-inspection agreement;
- Presence or absence of any suspected or actual adverse environmental condition or hazardous substance, including but not limited to asbestos, radon lead, mold, contaminated drywall, carcinogens, noise, or contaminants, whether in the building or in soil, water, or air;
- Decorative or cosmetic items, underground items, or items not permanently installed;
- Hidden, concealed or latent defects;
- Items not visible for inspection including the condition of systems or components which are not readily accessible; or
- Future conditions, including but not limited to, the likelihood of failure or the expected life of systems and components.

Additionally, Louisiana home inspectors **are not required** to:

- Offer warranties or guarantees of any kind;
- Calculate or determine the strength, adequacy, or efficiency of any system or component;
- Enter the under-floor crawl spaces, attics, or any area which, in the opinion of the home inspector, is not readily accessible;
- Operate any system or component that is shut down or otherwise inoperable;
- Operate any system or component that does not respond to normal operating controls;
- Disturb insulation, move personal items, panels, furniture, equipment, plant life, or other items that may obstruct access or visibility;
- Determine the effectiveness of any system installed to control or remove suspected hazardous substances;
- Project operating costs of components;
- Evaluate acoustical characteristics of any system or component;
- Inspect special equipment or accessories that are not listed as components to be inspected in this Chapter;
- Operate shut-off valves;

- Inspect detached structures, other than garages and carports;
- Inspect common elements or areas in multi-unit housing, such as condominium properties or cooperative housing;
- Dismantle any system or component, except as specifically required by these Standards of Practice;
- Disturb soil, snow ice, plant life, debris or personal items that may obstruct access or visibility; or
- Perform air or water intrusion tests or other tests upon roofs, windows, doors or other components of the structure to determine its resistance to air or water penetration.

Prohibitions

While a home inspector is not required to perform the aforementioned activities, there are certain activities that home inspectors are expressly prohibited by law from performing. Home inspectors **shall not**:

- Offer or perform any act or service contrary to law;
- Report on the market value of the property or its marketability;
- Report on the advisability or inadvisability of purchase of the property;
- Report on any component or system that was not inspected;
- Report on the presence or absence of pests such as wood damaging organisms, rodents or insects. However, the home inspector may advise the client of damages to the building and recommend further inspection by a licensed wood destroying insect inspector;
- Solicit to perform repair services on any system or component of the home which the inspector noted as deficient, significantly deficient or unsafe in his home inspection report for a period of one year from the date of the inspection.

There is an additional prohibition in the Louisiana Home Inspectors Licensing Law written specifically for home inspectors that are also **real estate licensees**. Specifically, **R.S. 37:1490** provides that a person licensed pursuant to the Louisiana Home Inspectors Licensing Law shall not engage in, or be financially compensated for, any home inspection that is part of a transaction in which that person receives a fee, commission, or other valuable consideration while acting as a licensee under the Louisiana Real Estate License Law, R.S. 37:1430 et seq. Acts 2010, No. 195, §1.

PURPOSE OF A HOME INSPECTION

Home inspections are a critical part of the home buying and selling process. Knowledge in the field of property inspection has become invaluable, especially in light of stricter legislation on both state and national levels. To make the process hopefully go smooth, it is the responsibility of the buyer's agent to:

- (1) Educate the buyer on the home inspection process and results.
- (2) Help the buyer sort through the inspection report and decide what to ask the sellers to repair. (This would be a good time to remind the buyer that the buyer is purchasing a used home. A buyer that wants to proceed with the contract after reviewing the home inspection report may be well advised to forego the "little" things and to stick with the major concerns.)

Likewise, it is the responsibility of the listing agent to educate the seller about home inspections and how a home inspection might impact the sale of the seller's home. Failure to do so may have a direct impact on whether or not the sale goes through.

Buyer's Perspective

Buying a home is typically the largest single purchase transaction the average person will ever make. To avoid, or at least minimize unpleasant surprises and unexpected difficulties, and to protect their financial commitment, a buyer will want to learn as much as possible about a house before they buy it. A home inspection may identify the need for major repairs, as well as the need for maintenance to keep it in good shape. After an inspection, the buyer will know more about the house, which will allow for informed decisions made with confidence.

One important feature to remember about home inspections is that **it is essential to the buyer to make an offer on a property subject to the results of the home inspection**. This indicates that, if the inspection reveals some major problems with the property, the offer can be withdrawn without penalty. We will take a closer look at this when we review the content of the Louisiana Residential Agreement to Buy or Sell that is relative to the home inspection process.

Value to buyers:

- A pre-listing home inspection establishes the condition of the property during the contract stage.
- Allows for cited issues to be addressed within inspection time parameters and before closing.

Seller's Perspective

A home inspection can identify problems in the making and suggest preventive measures that might help the seller avoid costly future repairs. Additionally, a home inspection can give a seller the opportunity to make repairs that will put the property in better selling condition to attract and entice potential buyers. A seller should be aware of any problems or issues that may lower the sale price, so that they can be addressed prior to the sale.

As a listing agent, you can list a property with confidence knowing that major concerns about the condition of a property have been addressed. You don't want to lose a potential buyer because *their* home inspector found things wrong that could have been repaired or replaced. Closing quickly and with fewer surprises is an obtainable goal with a home inspection.

Value to sellers:

- A pre-listing inspection helps establish any deficiencies that need repair prior to listing
- The printed inspection report available to the buyer on site reduces concerns prior to his making an offer.
- A complete inspection reduces potential risk for hidden defects found after the sale.
It also serves as a comparison to any buyer inspections.

Licensee's Perspective

Whether you represent the buyer or the seller, you will discover that making everyone familiar with the condition of the property before the sale eases tensions and builds trust during the sale process.

Value to licensee:

- A pre-listing inspection reduces problems related to this part of the transaction
- Any issues detected can be addressed prior to closing.

It should be noted that failure by a licensee to disclose a known material defect regarding the condition of real estate is a cause for censure, suspension or revocation of a license. Thus, if the licensee becomes aware of a material defect through a home inspection report, there is a duty to disclose such material defect.

THE REPORT

The rules and regulations of the Louisiana State Board of Home Inspectors require home inspectors to provide every client, or the authorized agent of the client, with a copy of the Standards of Practice and Code of Ethics for home inspectors before services are rendered. When this is not practical, copies must be attached to every completed inspection report.

Who Gets the Report?

Home inspectors are required to provide a written report of the home inspection to each person for whom the inspection is performed for compensation. The report must be provided **within five days** after the inspection has been completed. The home inspector is prohibited from disclosing inspection results or a client's personal information without approval of the client or the client's representative. Note that you must have written permission from your client to receive a copy of the home inspection report. This does not, however, give you carte blanche permission to further distribute the report.

What Can a Real Estate Licensee Do with the Report?

What you do with your client's home inspection report depends on the level of risk you are willing to take and the type of service you want to provide your clients. Remember that the report was prepared for a specific buyer. If the transaction falls through, the report effectively becomes outdated. Any future potential buyer should not have that report to rely on in determining the condition of the property. Having the report and using it for later transactions involving the property could lead to potential problems and liability on your part.

Remember that a home inspection experience is a confidential transaction between the home inspector and the person who purchased the report. The home inspector is liable only to the person who purchased the complete home inspection experience and report, NOT the other people that received a copy of the report from an agent. Providing your client with a report that was prepared for another buyer puts YOUR liability on the line – not the home inspector's, whose liability is contracted with the original client for whom the report was prepared.

As seasoned real estate licensees know, things can change in a minute during a real estate transaction, including the condition of a property. So, if you tell yourself that the report was just recently prepared, and you are considering passing it on to your next client, here is a word to the wise – PROCEED WITH CAUTION! (Oh, and one more thing – make sure your errors and omissions insurance premiums are up to date!)

RESIDENTIAL AGREEMENT TO BUY OR SELL

The Louisiana Residential Agreement to Buy or Sell contains language that is specific to home inspections. Completion of this section will almost certainly require an explanation, as it should, of the home inspection process and what the buyer can expect. This is especially true with first-time home buyers. From a liability perspective, your client should have a complete understanding of how the process works and what to expect. **In addition, the buyer should understand that the home inspection is not a stick with which to beat the seller over the head. While most buyers prefer to overlook the minor stuff, and to hand the major things over to their agents for negotiation with the listing agent and the seller, a buyer with second thoughts may want to use the results of a home inspection report to get out of a contract. It is your job to advise them on a reasonable course of action.**

CONCLUSION

Should a buyer have a home inspection? Yes. Do home inspections kill real estate deals? No. It is the job of the home inspector to inspect houses and write reports on what is found. If blame must be assessed, it is problematic houses that kill deals.

While you should always strive to give your clients the best possible service, you borrow real trouble by trying to be helpful in areas for which you are not qualified. Unless you are an inspector, lawyer, appraiser or an engineer, you should not try to take on their tasks and responsibilities believing that you are providing a service to your clients. "I don't know" is a valid response, especially when followed with "but I'll help you find out." You actually enhance your value to the client by being honest about your knowledge and helping them to locate the appropriate competent professional to answer their questions.

March 2, 2012

Inspection Date: March 1, 2012

Inspection No: 123456789

HOME INSPECTION REPORT

For
Mr. and Mrs. Prospective Buyer
6543 Any Street
Baton Rouge, Louisiana

PURPOSE OF INSPECTION: The general purpose of this limited, visual inspection, evaluation and report is to generally educate the clients about the general condition of the building being inspected, and to identify, for the client's knowledge, readily accessible, visible and apparent defects and/or conditions that, in the opinion, judgment and experience of the "Inspector", are not performing their intended function, without regard to life expectancy, on the date of the inspection, and which may adversely affect the function and/or integrity of the items, components and systems inspected, with the health and safety of the dwelling occupants in mind.

SCOPE OF INSPECTION: The limited, visual inspections, evaluations and reports for this building are intended for the exclusive use of the "Client(s)" only. The inspection is NOT an engineering evaluation of the property or structures, and will be performed in conformance with the minimal applicable "Standards of Practice" of the "Louisiana State Board of Home Inspectors." A copy of these standards, with the general limitations and exclusions, is included within the "Client(s)" report.

1. THE INSPECTION:

This inspection was held on March 1, 2012 and all of the utilities were turned on for the inspection. Attendees at the inspection were the inspector, the client and the selling real estate agent. The home was occupied with restricted accessibility for the inspection, and the temperature was approximately 80 degrees at the time of the inspection.

2. GENERAL INSPECTION OBSERVATIONS:

The inspection indicated a multi-story, single family residence on an asphaltic suburban street, of wood frame construction on an at-grade concrete and elevated pier and beam foundations, having a double detached garage. It is estimated that this original building is approximately 90+ years old. Multiple building additions and/or renovation have been added to the original structure. A non-code compliant apartment is installed above the living area of the house and contains a minimal living area and bathroom. Access to the apartment is granted via a wooden stairway and roof walkway installed in the rear of the building.

3. SITE INSPECTION:

An inspection of the Landscaping, Lawns and Grounds indicated that the vegetation was generally healthy and growing and that the ground generally slopes away from the building except along the perimeter of the front of the building. There were no trees in close proximity to the building, which were observed to be adversely affecting or impacting the structural performance. No canals or streams are adjacent to the property, and there was no evidence of high water or flooding apparent.

Incidental Concrete is the concrete poured without footings or subgrade preparation, being the driveways, walkway, porches and A/C slabs. Usually 3 ½" in thickness and without a sand bed or moisture barrier, and often without steel reinforcement, the incidental concrete is much more susceptible to "*shrinkage*", "*stress*", "*temperature*" and "*settlement*" cracks than the building foundation.

"Shrinkage" cracks are normal and due to the drying (*curing*) process when the concrete was poured and are generally of little significance as they usually penetrate only the mortar surfaces.

"Stress" cracks usually are caused by the application of loads greater than the concrete can support.

"Stress" cracks normally occur during the first few months after the slab is poured, while strength in the slab is low, and will typically become dormant with time.

"Temperature" cracks are normal and are caused by the thermal expansions and contractions within the concrete slabs.

"Settlement" cracks are usually due to the subsidence or consolidation of the soils underlying the building, and will normally extend completely through, and from edge to edge of the slab.

Concrete cracks are classed as either dormant (*cracking activity has ceased*) or active (*cracking activity may be expected to continue*). It is very probable to discover some degree of cracking in every incidental concrete slab. However, this is a normal occurrence, and unless specifically noted, the observation of "*shrinkage*", "*temperature*" or "*stress*" cracking will normally have only minor significance on the ability of the slab to support the normally applied loads. Of primary importance with these cracks is to seal the surfaces against water intrusion, and the potential for further damage. The degree of cracking observed in the incidental concrete is considered to be *about average*.

The driveway was surfaced with concrete. Walkways were surfaced with brick. The front and rear porches are constructed of brick and elevated wood with a brick patio, respectively. The left side porch is constructed with an elevated concrete slab. The rear porch has a wood framed roof covering installed above the porch. The incidental pavements appear to *typically* slope away from the buildings and the surfaces are *relatively* uniform and free from *significantly* cracked or missing areas.

There is an in-ground concrete swimming pool installed in the rear lawn that was not inspected. Wooden ornamental arbors and a wooden fence are installed in the rear lawn.

In the rear lawn, a pool house and exterior storage room are installed along the left property line and are attached to the garage.

4. BUILDING FOUNDATION and STRUCTURAL INSPECTION:

The foundation for this building is an elevated pier and beam system and an at-grade concrete slab at building additions on the front and right elevations of the original building. *During the inspection of the crawl space beneath the house, the inspector requires a minimum of 12 inches of clearance for access and sufficient clearance to "turn over" beneath the building, and does not crawl through standing water or open or hanging electrical lines. The inspector is not permitted to deflect or relocate water, gas or plumbing lines or ducts. In-accessible areas, such as listed above, were not inspected. The determination of the presence of, or damage caused, by termites, or other wood destroying insects or organisms, is specifically excluded from this inspection and report.*

The perimeter of the building has masonry foundation walls (*with vents*) located on the front and left sides. Accessibility to the crawl space for inspection is limited to openings approximately 10-12 inches high along the right sides. Portions of the available access have been blocked by screens, lattice, fencing, shrubs, ground soil levels, or other materials. *Portions of the crawl space beneath the house are in-accessible to a visual inspection, due to these and other restrictions.*

The *visible and readily accessible* components of the sub-structure were observed to determine apparent structural serviceability. In-accessible areas were not inspected.

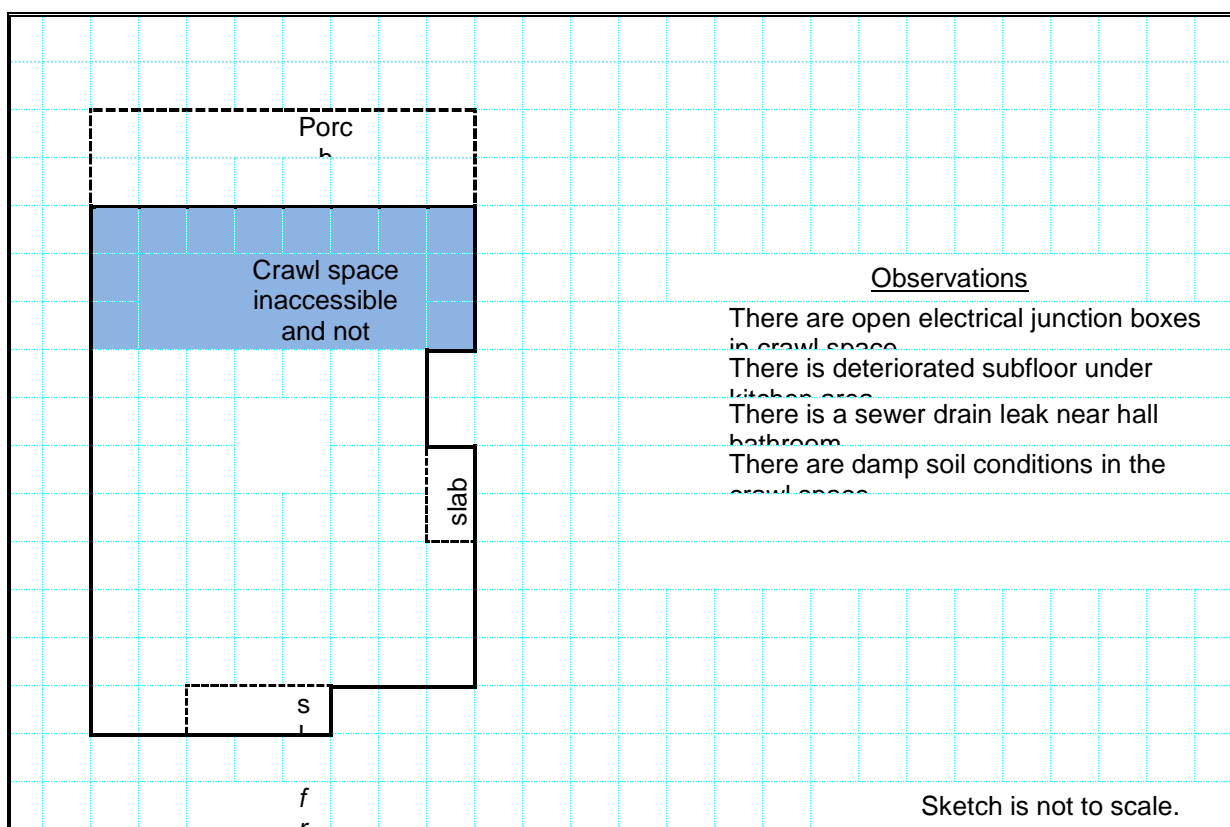
The brick masonry piers are approximately 12 - 16 inches high, and there are metal termite shields on the top of the piers. Resting upon the piers are wooden beams approximately 6" (*vertical*) x 6" (*horizontal*), extending about the perimeter and beneath some of the load bearing partitions of the house. The diagonally cut (*for stability*) wooden sub-flooring boards (*approximately 3/4" thick*) are set upon wooden 2" x 8" and 2" x 10" flooring joists at a typical 24" spacing. Cross bracing was observed between the joists. There was no insulation beneath the house.

Some of the inspected piers were tilted or settled slightly, as a result of soil settlements and due to movements and temperature expansions, however, the degree of deterioration observed is not considered to represent *significant structural failure* of the building's foundation. The settlement or the subsidence and consolidation process of the soils underlying the foundation may require up to 30 years completing, with the majority of the consolidation generally occurring within the first few years. Depending upon the composition, the percentage of voids and the moisture content of the underlying soils, the "settlement" may be dormant, or still active. The determination as to the expected amounts of residual settlements requires Geo-technical (*soils*) testing and analysis and is recommended. Some settlements can be attributed to water, either from drainage or water leaks, undermining and eroding the bearing of the foundation. *It is important to prevent drainage water from flowing beneath the house, in as much as is practical.*

These settlements are a probable cause of interior wall or ceiling cracking, or door and window separations or mis-alignments and floor un-levelness that may be observed. While this interior damage can be cosmetically repaired, there are no assurances that the building movements and settlements will not continue, as the causes are variable, and the repaired situation may return. If permanent repairs to the interior (*and exterior*) are essential, then it is recommended that the foundation be stabilized by a reputable foundation repair contractor.

Beneath the house, there are multiple electrical lines and water and gas plumbing lines. Some of the electrical lines hang loosely, and there are old styles of wires, with “fabric” (*armored cable*) insulation some of which may be frayed or damaged. During the life of this home, the electrical system has *probably* been updated, and some of these older wires *may* have been abandoned. The electrical system is likely to be a combination of original and updated wiring. This wiring beneath the house can be hazardous, and caution is urged in dealing with the electrical system of this house.

The galvanized plumbing lines are rusted, and the cast iron drains are a brittle material, presenting a leakage potential. The plumbing system appears to have been updated and/or repaired with PVC drain lines and copper and plastic water supply lines observed beneath the house as well. Particular locations of observed leaks in the plumbing system observed have been recorded in the inspection report summary, however under certain conditions, other leaks may be present.



With consideration to the vintage and style of construction of this house, the following recommendations, beyond the scope of this inspection, are offered:

- Have a complete, professional and independent termite and wood destroying insect inspection made on this house. Moist conditions, as exist under elevated structures, may promote insect activity.
- Have an electrical system safety inspection performed by a licensed electrician.
- Have a licensed plumber pressure test the plumbing lines (*especially the gas lines*) for leaks, and check any shower pans and tub drains for leakage.
- Prohibit rainwaters from draining, and ponding, beneath the house.

5. EXTERIOR INSPECTION:

This building is of wood frame construction with horizontal wood siding being the predominant exterior siding materials. The vapor retarder behind the exterior siding, if any, was not visible for inspection.

There are wood columns on this home, and these columns appear to be generally plumb and square with little evidence of *significant* deterioration visible.

The trim, fascias and soffit on this building are *typically* constructed of wood. These were visually inspected and found to be in *generally* serviceable condition. The exterior walls and trim *appear* to be serviceably sealed; *the caulk is generally poor, dry and brittle*. The exterior paint quality appears to be *generally* poor and becoming unserviceable. With the exception of those items that are specifically specified in the *inspection report summary*, the exterior items inspected were considered to be in *generally* serviceable condition.

The wooden and metal exterior doors are constructed with thresholds and weather-stripping. Wooden windows have been used on this building. Some of the wooden windows are fixed and do not open. The doors were inspected and were found to operate serviceably. The operable windows are painted closed and do not open.

INSPECTION FOR POTENTIAL MOISTURE INTRUSION:

Nearly all homes inspected have some minor exterior maintenance deficiencies. Of primary importance when maintaining your home's exterior is to keep the moisture out. Moisture that enters the building can cause wood deterioration and provides a damp environment that may attract wood destroying insects and provide conditions conducive for fungi (mold) growth. Interior wall cavities are concealed and are NOT included within the scope of in this inspection or report. If wood deterioration due to the potential of moisture intrusion is noted in the inspection summary or, if water stains were observed in the interior of the building, we recommend that a mold sample be conducted to identify potential contaminants. *Note that the inspection or the reporting of, the presence or the concealed damage due to, wood destroying insects or mold is not within the scope of this inspection or report.*

To reduce the amount of "*moisture intrusion*" into the building, the exterior should be completely and properly sealed. During the course of this inspection, the following were inspected for proper "*moisture intrusion*" reduction;

- The ground soil levels should be maintained 4 to 8 inches below the bottom of wood siding, the brick and the top of the foundation slab.
- Prevent vegetation and planting beds from growing into, or over, bottom of wood siding, the brick and the top of the foundation slab.
- The weep holes at the bottom of the brick allow condensate to drain from the air space, and should be free or debris.
- The gaps and openings around the doors and windows and at the different material joints and penetrations should be completely sealed and caulked, with the caulk being pliable without gaps or voids.
- Door weather-stripping and thresholds should be completely sealed and caulked, with the caulk being pliable without gaps or voids.
- The vertical joints in horizontal exterior siding should be completely sealed and caulked, with the caulk being pliable without gaps or voids.
- A good weather protective paint or varnish finish should be maintained on exterior wood.
- Much of the decorative exterior wood trim is not treated wood, and should be completely painted and sealed and caulked, with the caulk being pliable without gaps or voids, if replacement of the trim becomes necessary, paint the backside and ends of the wood before installing.
- The roofing shingles should be pliable and without cracked, curled and loose or broken shingles.
- The gaps and openings around the roof penetrations and flashings, should be completely sealed and caulked, with the caulk being pliable without gaps or voids.
- Drip edges at the roof edge will help direct water away from the wood fascias and soffits.
- Gutters and downspouts should be kept clean and leak free to direct water away from the wood fascias and soffits.
- Proper ventilation is important in reducing moisture in the attic and crawl spaces
- Firewood or debris should not be stacked against the building and there should be no wood in contact with the foundation slab perimeter.

Additionally, the following have been observed:

- ☑ Wood deterioration, due either to "*wood-destroying insects*" or "*moisture damage*", have been observed as described in Section A of the Inspection Report Summary.
- ☑ Evidence of apparent "*moisture intrusions*" on the interior have been observed as described in the Inspection Report Summary.

It is recommended that deficiencies be serviceably repaired, and that the client(s) have an independent inspection for wood destroying insects and organisms preformed.

6. ROOF COVERING, FLASHINGS, GUTTERS and DOWNSPOUT INSPECTION:

Asphaltic or fiberglass shingled composition roof surfaces *typically* exist in one of three stages during their functional life:

1. In the first or earlier stage, the shingles are generally pliable and flat. Shingles in this stage are indicated as being in “**good**” condition, and this period will normally range from the initial installation to about 4 to 6 years.
2. When the shingles begin to become “brittle”, or to “crack and split” or “curl” at the edges, they are considered to be in the second stage, and are rated as being in “**fair**” condition. This period may typically begin as early as 3 to 5 years and extend through 8 to 12 years. These shingles may be readily damaged by falling debris or limbs, and once “cracked or split”, occasional leakage can occur in spot areas. The roofing nail heads may also begin to “pop” and become exposed through the shingles. Some maintenance may be required to seal the “cracks and splits” and the “popped” nail heads. The functional life of the roof surface may be extended by not walking on these brittle shingles.
3. In the final and last stage of the shingle’s functional life, the shingles become brittle, cracked, curled and cupped. Bead loss, evident on the ground and in the gutters, is another indication that the shingles have reached this stage. Roofing surfaces which are in this final stage are indicated as being in “**poor**” condition, and may be easily damaged by wind and rain, and leakage may occur at any time, indicating that the replacement of the shingled roofing surface will be justified.

The **roof** on this structure is pitched and gabled on the original roof and portions of the building additions and low-sloped over the rear porch and front foyer region. The roof covering material is primarily Architecturally Styled fiberglass shingles. The manufacturer’s suggested *normal* life expectancy of this type of roof covering may be from 25 to 30 years, when properly maintained. However in Louisiana, with the hot sun and wind driven rains, a life expectancy from 22 to 25 years would be more realistic. There is a rolled asphalt roof covering system over the low sloped roof systems with these types of roof covering typically having a 12 to 15 year useful life expectancy, with proper maintenance. Clay tile ridge caps are installed. On the rear porch, a standing seam, metal panel roof covering is installed. This type of roof covering may last 30 to 40 years depending on quality of material used and proper maintenance.

Our region of the country often experiences high intensity wind driven rains, which *can* penetrate a roof surface in any of these conditions. The necessary ridge, gable and turbine vents and the plumbing and gas vents and flashing are all susceptible to water intrusion during these weather conditions.

There are some shingles manufactured which have longer life expectations, and factors such as a southern exposure, shaded areas and wind breaks can create varying conditions of the shingles on the same roof. *The flashing around fireplaces, vent pipes and other roof penetrations can also deteriorate with time, and require periodic maintenance such as recaulking or sealing. For older roofs, it is recommended that a repair proposal for a leak free roof be obtained from a reputable roofing contractor.*

The roof surface on this building has an *estimated* and *approximate* age of years and the condition is considered to be poor; the shingles are curled, cracked and brittle, and the condition is commiserate with the age of the shingles. *The roof appears to be at the end of its useful life.*

Attic ventilation is provided by gable vents. The valley roof flashing is galvanized metal. Both chimneys are of masonry construction. The front chimney does not have a functional damper and is open to the exterior. Each chimney has a cap at least two (2) feet above the roof ridge line or approximately eight (8) feet above the roof line. It *appears* that the roof protrusions are *generally* properly flashed and the vents properly penetrate the roof and appear to be sufficiently sealed. There are overhanging tree limbs requiring trimming. The roof inspection was performed accessing the roof surface with an exterior stairway.

7. ROOF STRUCTURE, ATTIC and INSULATION INSPECTION:

The inspection of the **attic** provides information concerning the quality of construction and the structural integrity of the building as well as exposing potential fire or safety hazards and possible electrical and plumbing system deficiencies. The insulation in the attic is composed of blown fiberglass insulation approximately 6 to 8 inches thick. *(Insulation manufacturer recommendations for attic insulation in Louisiana are a value of R-30, which is approximately 8” to 9” of insulation.)* Insulation that has settled will have lost some of its insulating abilities. The vapor retarder beneath the insulation, if any, was not visible for inspection. The heating and cooling ductwork in the attic is insulated and supported. There are no *apparent* blocked air vents and the plumbing vent pipe joints appeared to be tight and secure.

The *readily accessible* and *visible* wooden structural components of the roof and ceilings, being the ridge beams, roofing rafters, sheathing, supports and ceiling joists, were observed. The condition, material sizes and spacing *appeared* to be *generally* adequate to support the normal dead loads and the applied live loads and wind forces to which this structure may be *normally* subjected unless otherwise noted in the inspection summary report.

8. DOUBLE DETACHED GARAGE INSPECTION:

The double detached garage is constructed with concrete flooring and has an attached storage room. The exterior siding is horizontal vinyl siding and horizontal wood siding and roofing materials are the same as the main building and the floor is depressed from that of the main building and there is a switched overhead light.

The garage door is of metal material and the door springs, rails and locks *appear* to be safe and functioning properly. There is no weather-tight gasket at the bottom of the garage door; evidence of water intrusion was evident near the door. The Craftsman automatic door opener *appears* to function safely and serviceably, and reverses upon meeting reasonable resistance.

Comments concerning compliance to **Governmental Building Codes and Regulations** are not within the scope or standards of practice of this inspection. The building codes and regulations are “*dynamic*” and change frequently, *however*, providing that a component complied with the applicable codes and regulations at the time of original installation, and has not been significantly modified since original installation, then that component is considered to be in compliance with the codes and regulations, *unless*, renovations, remodeling or additions have occurred which affect the component. Examples are:

1. Current plumbing codes require floor mounted, gas fired, water heaters to be elevated a minimum of 18 inches above the floor.
2. Current electrical codes require that electrical receptacles within 6 feet of water service be GFCI (*Grounded Fault Circuit Interrupter*) device protected.

Renovations, remodeling or additions must comply with the codes and regulations which are applicable and the time. In performing a home inspection, it is not possible to determine the time periods of modifications or of the codes and regulations which were in effect at the time of the modification.

9. ELECTRICAL SYSTEM INSPECTION:

The electrical system inspection noted that the electrical service is underground and that the electrical power is provided with a 200 amp, 240-volt service. The main service panel is located in the right exterior wall and has circuit breakers. There is an exterior sub-panel providing service to the air conditioning equipment and an exterior branch panel adjacent to the main panel. A pool pump electrical panel is installed near the pool equipment.

During the exterior electrical inspection, the following were inspected and found to be serviceable *except as noted in the inspection report summary*.

- A copper ground rod and a secure grounding connection.
- The service entrance galvanized conduit was inspected and observed to be generally serviceable.
- Exterior receptacles have weather resistant covers and accessible receptacles inspected and tested, were *generally* properly “hot” and grounded with the correct polarity *except as noted in the summary*.

Noted during the interior electrical inspection; the following representative number of accessible switches, receptacles and components were inspected and found to be serviceable *except as noted in the inspection report summary*.

- Light circuits *randomly* tested, were *generally* operational.
- Accessible receptacles inspected and *randomly* tested, were *generally* properly “hot” and grounded with the correct polarity *except as noted in the inspection report summary*.
- For Client’s Information: The original electrical service provided in this residence was an “un-grounded” 2 wire system, which has been updated by the utility company to a three wire grounded service. There is a combination of the original wiring and updated grounded wiring in evidence. There are the original 2 prong receptacles, which are not grounded, and there are 3 pronged receptacles in the 2 wire system, and some of these 3 pronged receptacles are not grounded. This is a normal condition in homes of this vintage, and it is in general conformity with the prevailing codes.
- GFCI (*Grounded Fault Circuit Interrupter*) device protection is provided.

GFCI (Grounded Fault Circuit Interrupter) device protection was available, but was not generally required by the building codes until approximately 1987. Any references to GFCI devices are informational only. Further information pertaining to the electrical system inspection may be found in the *inspection report summary*.

Aluminum branch circuit wiring was permitted in residential construction during the approximate 1965 to 1973 time period. Aluminum wiring for the utility company service and for the 220 volts appliances and heaters is generally permissible. Aluminum branch circuit wiring was not observed during this inspection, however, that does not preclude the possible existence of aluminum wiring in this structure.

10. PLUMBING SYSTEM INSPECTION:

The plumbing system was inspected to determine the adequacy and the serviceable operation of the components and to detect any *visible and apparent* water leaks. The toilet(s) *appeared* to flush and refill within 60 to 90 seconds. The lavatories, tubs and fixtures *appeared* to drain serviceably, and faucets (both hot and cold) have a serviceable water flow. The lavatory pop-ups and the tub drains (*when installed*) *appeared* to be serviceable. There were no significant *visible or apparent* plumbing system deficiencies observed, *except as noted in the inspection report summary*.

NOTE: The gaskets and sealing materials in "older" plumbing fixtures, such as in this house, can deteriorate over time. The plumbing system comments contained in this report are valid only as of the day of the inspection. Latent defects or deficiencies in plumbing fixtures and piping that are not readily visible or accessible during the inspection are excluded from the scope of the inspection. Older houses may have deteriorated lines beneath the slab or ground soil level of pier and beam houses, for example, that are not readily visible for inspection. Should the client be concerned about concealed or inaccessible plumbing lines, a plumbing inspection of the sewer line interiors by a reputable, licensed plumbing contractor is recommended.

The tank type water heater is a gas fired RUUD (*unknown age*) unit having a 40 gallon water tank capacity. A pressure temperature relief valve is located on the tank, as required. There was a collection pan under the water heater.

A second tank type water heater is an electric RUUD (1981) unit having a 20 gallon water tank capacity.

A pressure temperature relief valve is located on the tank, as required. There was no collection pan under the water heater.

There was a draft diverter on the gas unit, and no air flow could be felt during operation. Ventilation *appears* to be adequate and the gas piping was black iron, with a flexible gas piping connection to the heater and there is a gas shut-off valve near water heater. The pilot light appeared to be functional and the burner did not have any *visible* evidence of excessive corrosion, dust, flaking or cracks.

The hot and cold water supply pipe material is copper, plastic PVC, plastic PEX and galvanized iron and the water temperature produced at the faucets was sufficiently hot. The drain piping system appears to be constructed primarily with cast iron and PVC piping materials. The water heater appeared to function serviceably, and there was no *visible* evidence of current leakage except as noted in the inspection summary report.

11. HEATING (HVAC) SYSTEM INSPECTION:

The heating and cooling systems commonly referred to, as the "HVAC" system (*heating, ventilating and air conditioning*) is comprised of two central heating and cooling system(s). The inspection of the heating and cooling system is limited to a determination of *generally* serviceable operation, as of the date of the inspection. This inspection is not a determination of the remaining service life expected from the system components or of compliance to Governmental Building Codes or Regulations. Temperatures were approximately 80 degrees at the time of the inspection.

SYSTEM #1: Front

Heating is provided by a gas fired "Consolidated" (1995) "forced air" horizontal furnace with an input capacity of 60,000 BTU. The inspector observed that the fan and the thermostat both *appear* to operate serviceably and that the ductwork is supported and insulated.

The gas-fired furnace *appears* to be vented adequately and the gas piping is black iron with flexible gas piping connections. There is a gas shut-off valve near the furnace and the thermocouple and pilot light *appear* to be serviceable.

SYSTEM #2: Rear

Heating is provided by a gas fired "forced air" horizontal furnace with an unknown input capacity. The heater was inaccessible due to attic framing and HVAC ducts. The inspector observed that the fan and the thermostat both *appear* to operate serviceably and that the ductwork is supported and insulated.

12. AIR CONDITIONING (HVAC) SYSTEM INSPECTION:

SYSTEM #1: Front

Cooling is provided by an electrical split system "York" *unknown age* air conditioner with an approximate capacity of 36,000 BTU, which is equivalent to 3 TONS. The "Allstyle" (*unknown age*) evaporator coils have a capacity of 3 TONS. Conditions permitting, the inspection of the system included a determination of acceptable electrical current drawn by the compressor, and a temperature drop across the evaporator coils to determine acceptable refrigerant levels.

The exterior Compressor/Condenser unit was mounted on a flat stable surface with an electrical disconnect within reach. It was *generally* clean and level and operating smoothly and quietly.

The interior evaporator coils were *generally* clean and had a condensate drain pan with a float shut-off control. During the unit's operation, it was observed that the refrigerant level was *apparently* serviceable. It appears that the cooling system is operating serviceably.

SYSTEM #2: Rear

Cooling is provided by an electrical split system "York" 2004 air conditioner with an approximate capacity of 48,000 BTU, which is equivalent to 4 TONS. The evaporator coils were inaccessible due to attic framing and HVAC duct installation. Conditions permitting, the inspection of the system included a determination of acceptable electrical current drawn by the compressor, and a temperature drop across the evaporator coils to determine acceptable refrigerant levels.

The exterior Compressor/Condenser unit was mounted on a flat stable surface with an electrical disconnect within reach. It was *generally* clean and level and operating smoothly and quietly. During the unit's operation, it was observed that the refrigerant level was *apparently* serviceable. It appears that the cooling system is operating serviceably.

It is recommended that the Heating and Cooling Systems be professionally serviced and cleaned annually to provide more efficient operations and to help extend the service life of the components. The "*cloth duct tape*" often used in the attic to seal the duct, plenum and transition connections will deteriorate over time, and create inefficient air leakage into the system. Clean filters are necessary for efficient operation and should be changed at least monthly.

- The Cooling System components should be serviced and the components cleaned and checked for air and refrigerant leakage and the system properly charged with refrigerant and oil prior to the *cooling season*.
- Prior to the *heating season* the Heating System should be serviced and the components cleaned and checked for air leakage, with any rust removed from the heat exchanger (*gas fired systems*) and the burners, and the unit checked for defects in the heat exchanger.

13. INTERIOR INSPECTION:

The interior rooms inspected were the:

- living and dining areas
- den
- kitchen
- 3 bedrooms
- 3 bathrooms
- foyer, hallways, storage and laundry rooms
- apartment
- pool house

Visually inspected in these rooms were the composition and condition of the ceilings and walls (*typically gypsum dry-wall*) and flooring together with the operation of exterior doors and a *representative (random)* number of the windows. The presence of HVAC registers and a switched, overhead light was observed in each room and the location, grounding and polarity of a *representative (random)* number of accessible electrical receptacles was evaluated, as was the operation of ceiling fans. In addition to the items listed above, in the kitchen and baths the cabinets, countertops and the water flow (*hot and cold water*) were inspected. The electrical receptacles within 6'

of water services were inspected for **GFCI** devices and the plumbing was inspected for any *visible and apparent* water leakage evidence. In the bathrooms, the inspection included heaters, exhaust fans and ventilation, as well as the operation of installed plumbing fixtures. The presence of smoke detectors was not observed.

Please be aware that the use of "lead based" paint was permitted for homes built until about 1978. Testing for and the detection of the presence of "lead based" paint is beyond the scope of this home inspection. Should the possible presence of "lead based" paint be of concern for your family, and the age of your home falls within this time period, professional testing facilities are available which can confirm the presence of "lead based" paint.

In the kitchen, the operation and serviceability of the built-in appliances and equipment was evaluated, and with the exception of those items specifically listed in the *inspection report summary*, the items inspected were considered to be *generally* operating serviceably at the time of this inspection:

- **Jenn Air** Cooktop
- **Jenn Air** Oven
- **Jenn Air** Exhaust fan and light
- **Kitchen Aid** Dishwasher
- **ISE** Disposal
- **Sub-Zero** Refrigerator

The inspection of each fireplace and chimney disclosed a fireplace constructed of masonry with a damper. Some nominal cracking in the brick is a normal occurrence, and is not considered to be a significant fire hazard unless noted in the *Inspection Summaries*.

The stairways on the exterior of this building are surfaced with wood and the steps are *generally* uniformly spaced without *substantial* dimensional variances. The nose should be (*by current code requirements*) a maximum of 1", the tread width a minimum of 10" (*with the nose*), and the riser height a maximum of 8 ¼". This stairway *generally* meets these requirements. There is a handrail with the top of the handrail located between 30" to 36" above the treads.

14. REPORT OF THE BUILDING'S GENERAL CONDITION:

Based entirely upon the *readily accessible, visible and apparent* aspects of this inspection, this building is considered to have been originally constructed in a manner which *generally* conformed to the *minimum* construction material and skill standards ordinarily practiced by reputable contractors in this locality, at the time it was built. The *readily accessible, visible and apparent* observations indicate that this building is *generally* in serviceable condition, commiserate with the age of the building, and that the depreciation that has been allowed, and the degree of care and maintenance exhibited are below normal, for the age of this building.

15. INSPECTION SUMMARY REPORT:

During the course of this home inspection the below listed components and items were determined, in the opinion of the Inspector, to be un-serviceable or un-satisfactory. Should any *significant* deficiencies in the "components" or "mechanical systems" be reported, it is recommended that reputable and licensed contractors be engaged to provide repair proposals for properly operating "components" or "mechanical systems".

A. Deficiencies and Defects of Component Materials: There were no *visually or readily apparent or significant* component deficiencies or material defects observed, except:

Wood deterioration, due either to "*wood destroying insects*" or "*moisture damage*", was observed at the following locations:

- ☐ On the exterior stairway and wooden handrail of the roof walkway, the rails and lattice panels are deteriorated in random areas.
 - ☐ The garage door trim is deteriorated.
 - ☐ On the rear exterior storage room, the siding and trim are deteriorated.
- ☐ There are multiple locations where the lap siding on the left side elevation wall near the wall offset is deteriorated.
 - ☐ The siding near the left side porch is deteriorated.
 - ☐ The siding at the bottom of the left side wall is deteriorated.
 - ☐ The bottom of the front door is deteriorated.
 - ☐ The siding, trim and wall features below the dining room window are deteriorated.
 - ☐ The bottom of the front porch siding is deteriorated.

- ☐ The bottom of the right elevation wall siding is deteriorated.
- ☐ The structural beams of the rear porch are deteriorated in three locations.
- ☐ The fascia at the rear elevation of the pool house is deteriorated.
- ☐ The subfloor beneath the kitchen floor is deteriorated.
- ☐ Wooden framing material is in contact with the driveway sidewalk near the garage.
- ☐ There are rust stains at nail locations of the exterior lap siding on the left elevation walls. It appears that the wrong type of nail was used to secure the siding.
- ☐ There is plant growth on the front left roof covering (shingles). There are tree limbs in contact with the roof. The valley flashing does not properly extend past the fascia on the left side of the house. The asphaltic roof surface condition is considered to be poor; the shingles are curled, cracked and brittle. *The roof appears to be at the end of its useful life.*
- ☐ There appears to be water intrusion through the walls and doors into the garage. There is no weather-tight gasket at the bottom of the garage door; evidence of water intrusion was evident near the door, as well.
- ☐ There is a roof leak over the rear storage room and evidence of water intrusion into the room.
 - ☐ Due to the multiple roof breaks and attic configuration, poor attic ventilation is present.
 - ☐ There is water damage to the baseboards of the right side master bedroom near the doors.
- ☐ In the rear master bedroom, there is a pronounced floor deflection. The conditions associated with this circumstance are unknown as the crawl space in this region was inaccessible.
 - ☐ There are sloping floors throughout the house.
- ☐ The rafters supporting the rear porch roof are undersized creating deflection in the structural members.
- ☐ The front den fireplace is open without capability of closure; the unit is in need of repair prior to use.

B. Inoperable Systems or Equipment: Mechanical equipment and systems inspected were observed to be in *generally* serviceable operating condition, except:

Electrical System: (from the operation of a representative number of accessible components)

For client's information: *The original electrical service provided in this residence was an "un-grounded" 2 wire system, which has been updated by the utility company to a three wire grounded service. There is a combination of the original wiring and updated-grounded wiring in evidence. There are the original 2 prong receptacles, which are not grounded, and there are 3 pronged receptacles in the 2-wire system, and some of these 3 pronged receptacles are not grounded. This is a normal condition in homes of this vintage and is in general conformity with the prevailing codes. "Tube and knob" wiring evidence was observed in the attic.*

- ☐ Electrical receptacles do not appear to be operational in the sunroom.
- ☐ There is an open electrical junction box near the light of the pool house.
- ☐ In the pool service panel, the capacity of the panel is questionable due to the amount of service loads imposed. The condition should be evaluated by a licensed electrical engineer. The pool panel cabinet is rusted.
- ☐ In the main service panel, there is an improperly terminated service wire; there are rusted breaker/wire connections; there is a missing fastener for the interior dead panel cover.
- ☐ The secondary service panel is inaccessible for inspection due to restrictions by the air conditioning condenser unit. The cover panel is loose.
- ☐ There are open electrical junction boxes at the right side wall near the rear porch, rear storage wall, the attic, and beneath the house.

Plumbing System:

- ☐ In the utility room, the waste plumbing vent does not properly extend over the roof, as required.
- ☐ In the pool house, the sink drain line is not properly vented.
- ☐ In the front master bathroom, the toilet is loose. There is corrosion of the tile and wall of the shower.
- ☐ There is a water leak on the right elevation, hose bib.
- ☐ There is a sewer drain leak beneath the hall bathroom.

Appliances:

- ☐ The service water piping at the water heater in the pool house is not properly installed.
- ☐ There is rust on the service piping and gas vent of the front water heater.

C. Items in need of "Eventual" Maintenance: There were no *visually apparent or significant* "eventual" maintenance requirements observed, except:

- ☐ The exterior siding is cracked and split on the rear elevation wall of the apartment.
- ☐ There are cracked windowpanes on the left side of the house.

- ☐ There are damp soil conditions in the crawl space beneath the house. Consideration of the installation of a plastic sheet material is recommended to restrict moisture release from the soil.
- ☐ The ground slopes beneath the house around the front of the building.
- ☐ Vines, shrubs and trees are in contact with the exterior façade. Where practical, remove the vegetation a nominal 2 feet to allow moisture to dry along the perimeter of the house.
- ☐ The walls of the house appear to be conducive to water retention due to the environment and physical construction. Where practical, we recommend that you develop a water management plan to mitigate water damage.
- ☐ Due to the age and condition of the plumbing materials in the crawl space, we recommend that a pressure test be performed on the gas and water lines and a hydrostatic pressure test be performed on the sewer line to verify integrity of the lines.
- ☐ The exterior paint condition is poor and becoming un-serviceable.
- ☐ The exterior caulk is generally poor, dry and brittle.

D. Other Observations:

- There are water stains on the ceiling of the pool house.
- The building water supply valve is located on the front lawn.
- The gas service valve is located on the right side of the building.
- There is a ceiling patch in the rear master bathroom.
- Aluminum paint was observed on the attic framing near the rear fireplace; this condition is typical in applications after a fire.

E. Items observed and considered to be NORMAL in the aging process of this home:

- The wooden columns were observed to have normal material drying cracks.
- The roof surface was observed to have some normal unevenness.
- The attic insulation is settled.

F. Moisture Intrusion: The client(s) are referred to the body of the report section pertaining to “Inspection for Potential Moisture Intrusion” in Section 5, Exterior Inspection. Items such as eave deterioration, ceiling and wall stains, and fungi odors or growth are representative of water entry into the building and may require further intrusive investigations.

G. Components that were NOT inspected: (See limitations and exclusions)

- Sub-surface components; sprinklers, fountains, yard lighting, drainage systems, detached structures, decks or patios and intercom, security, or audio systems were NOT inspected.
- In-accessible areas NOT inspected include; interior cavities of walls, areas obscured by stored or personal belongs (*ie: attics, closets and storage areas*), and areas with accessibility limitations such as the exterior edges of attics.
- The apartment and associated bathroom were not inspected due to restrictions by personal items.
- The left side of the garage, pool house and exterior storage due to inaccessibility from fencing materials.
- The rear HVAC equipment in the attic due to attic framing and ducts.
- The swimming pool was part of this agreement.
- Regions of the crawl space shown on the attached sketch due to restrictions by framing, lattice, and low ground clearances.

These suggestions are offered to benefit the clients; they have no reflection on the condition of the inspected building.

I. Informational Suggestions:

- Check the lot survey to verify the F.I.R.M. Flood Plain designation. (F.I.R.M, Federal Insurance Rating Map)
- Professional, independent wood destroying insect and organism inspection and certificate should be provided by the seller.

II. Convenience Suggestions:

- The buyer should replace the smoke (and carbon monoxide) detector batteries upon occupancy, and semi-annually thereafter. (Regular daylight saving time changes are good times.)
- The buyer should replace the central HVAC filters, upon occupancy, and at least monthly thereafter.

III. Safety Suggestions:

- For safety, it is suggested that buyer have GFCI (Grounded Fault Circuit Interrupter) devices be installed at all locations within 6 feet of all interior water service locations and on all receptacles in bathrooms and on an exterior receptacle. (This is the current Electrical code requirement)

- Any tripping hazards should be eliminated.
- If the furnace is a gas (or propane) fired system, a deteriorated heat exchanger can emit harmful carbon monoxide gases. It is therefore suggested that the gas fired furnace and heat exchanger be completely inspected and tested on an annual basis, prior to the heating season. For safety, it is suggested that the buyer install a Carbon Monoxide Detector, a device similar to a smoke detector, with a moderate cost.

END OF HOME INSPECTION REPORT

If you should have any questions regarding this report, please contact our office.

Best regards,

Home Inspector Signature

Home Inspector Name

LHI No. 54321

APPRAISALS

Learning Objectives

Upon completion of this lesson, you should be able to:

- Understand a lender's perception of value
- Recognize the appraisal process
- Identify the three types of appraisal methods
- Know how Regulation Z applies to appraisers and appraisals

Introduction - Appraisals

After qualifying the borrower, the underwriter must then qualify the property being purchased

Is property worth enough to serve as collateral for the loan?

Lender's Perception of Value

- Underwriters rely on appraisals for estimates of market value. The appraiser will analyze the property and issue an objective estimate of its market value.
- Widely accepted definition of market value:
 - "The most probable price which a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus"

Home Valuation Code of Conduct - HVCC

The HVCC was created to enhance the integrity of the home appraisal practice in the mortgage finance industry. The HVCC dictates certain guidelines that must be followed by lenders to sell loans to protect undue influence in the appraisal process:

- Communication between lender and appraiser is limited
- Appraisal can be transferred only if original lender assures compliance with HVCC
 - Although some lenders will not allow this
- Lenders also cannot:
 - Request or provide a desired value
 - Give a target amount
 - Provide comparables to the appraiser
 - Accept an appraisal who is affiliated in any way with the lender
 - Participate in the selection of the appraiser
 - Get a second appraisal
 - Unless first appraisal is flawed
- Borrowers must be provided with a copy of the appraisal
 - No less than 3 business days prior to closing

HVCC applies to:

- Any mortgage loan sold to FNMA or Freddie Mac
 - Does not apply to FHA or VA
- HVCC has standards established for:
 - Solicitation
 - Selection
 - Compensation
 - Conflicts of interest
 - Appraisal independence

Appraisals and LTV Ratios

- Lender uses property's appraised value to determine how much money to loan with property as security
- Loan-to-value ratio expresses relationship between loan amount and property's value

LTVs and Risk

- LTV affects:
 - Risk of default
 - Risk of loss if foreclosure is required
- Lower LTV = Lower Risk
- Lenders use LTVs to set maximum loan amounts
 - LTV rules applied depend on what type of loan is being applied for

Loan Based on Sales Price/Appraisal

- Maximum loan amounts are based on either:
 - Sales price, or
 - Appraised value
 - Lesser of the two

Collateral vs. Creditworthiness

- Lenders have become more willing to make loans with high LTV ratios
 - Rely more on creditworthiness of borrower than value of property
 - Stricter qualifying standards

Appraisal Standards

An accurate appraisal is essential to the element of loan underwriting.

- If property is overvalued, loan amount will be larger than it should be and lender's risk of loss is greater
 - Appraisals help lenders determine, in the event of foreclosure, can the property be sold to satisfy the debt?

In 1989, Congress passed Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA)

- Provisions prompted states to pass licensing and certification legislation for appraisers
- Appraisals used in "federally related" loan transactions must be:
 - Prepared by state-licensed or certified appraisers
 - In accordance with uniform standards of professional appraisal practice
- "Federally related" loan is one made by any bank or savings and loan association that is regulated or insured by federal government
 - Some states have made licensing and certification mandatory for all appraisers

The Appraisal Process

- Real estate appraisal generally involves:
 - Define problem
 - Determine data needed

- Gather and verify general data
- Gather and verify specific data
- Apply appraisal method
- Reconcile results
- Issue an appraisal report

Defining the Problem

- In this step, appraiser identifies property to be appraised (subject property)
- Appraiser also:
 - Determines purpose of appraisal
 - Specifies “as of” date

Determining Data That is Needed

- Data required depends on what type of property is being appraised
- Two general categories of data:
 - General data
 - Specific data

Gather & Verify General Data

- “General data” refers to information about factors outside property that affect property’s value. May include:
 - Region’s economy
 - Neighborhood information

Gather & Verify Specific Data

- “Specific data” refers to information about property. May include:
 - The site
 - The house
 - Other site improvements

Apply the Appraisal Methods

- Appraiser applies each of three methods to get three separate value indicators
 - Each figure is indication of property’s value

Reconcile the Results

- In reconciliation, appraiser weighs value indicators and decides on final estimate of subject property’s market value

Issue the Appraisal Report

- Last step is to prepare appraisal report, which presents value estimate and summarizes supporting data

The Appraisal Process

- Depending on property, appraisers gather data about site through in-person inspection
- A “drive-by appraisal” is sometimes all a lender requires
 - Appraiser pays a brief visit to property after gathering info from other sources

Appraisal Methods

- Three ways to appraise real estate:
 - Sales comparison method
 - Replacement cost method
 - Income method

Sales Comparison Method

- “Sales comparison method” uses sales prices of comparables to estimate market value of the subject property
 - Preferred by appraisers

Sales Comparison vs. CMA

- “Competitive market analysis” (CMA) is informal version of sales comparison method of appraisal
 - Used by real estate agents
 - May use current and expired listings
 - Appraisal is based on actual sales

Identifying Comparables

- Sales make better comparables than listings. When appraiser is choosing comparable, she is concerned with:
 - Date of sale
 - Location of property
 - Physical characteristics of property
 - Terms of sale
 - Whether sale was arm’s length transaction

Date of Sale

- Sale should be within the past 6 months because it is a more accurate reflection of current marketplace
 - Need 3 comparables
 - Comparable sales should never be more than a year old
 - Adjustment for sale over 6 months old
- A comp sold ten months ago for \$277,000. Local properties values have risen by 3% over the past 10 months. Therefore, the comp should be worth approx. 3% more than it was 10 months ago.
\$277,000 value ten months ago
x 103% inflation factor
\$285,310 approximate present value

Location of Sale

- Comparables should be from neighborhood where subject property is located
- If there aren’t any, appraiser can look elsewhere in comparable neighborhoods
- Make appropriate adjustments

Physical Characteristics

- Comparable property should have physical characteristics similar to those of subject property
- Comparable’s price adjusted to indicate value of subject property:
 - Down if subject lacks feature
 - Up if subject has extra feature
- Example #1:
Comparable is similar to subject property
Some differences
Subject – 2 car garage & comp – 1 car garage
Appraiser estimates 2-car garage adds \$2,400
Comp sold for \$223,500 + \$2,400
This will reflect the fact that the subject property has more garage space than comp

- Example #2:
 Comparable is similar to subject property
 Some differences
 Comp has a fireplace & subject does not
 Appraiser estimates a fireplace at \$1,100
 \$1,100 is subtracted from comp's price
 This will reflect the fact that the subject property has no fireplace

Terms of Sale

- Appraiser must take into account influence terms of sale may have had on price paid for comparable property
 - Special financing may make borrower willing to pay more for a property
- USPAP requires appraiser to state whether estimate is in terms of cash, or other financial arrangements

Arm's Length Transaction

- In "arm's length transaction":
- Both parties are fully informed
- No unusual pressure to act
- Property was on open market for a reasonable amount of time

Sales Comparison Method - Adjustments

- Appraiser rarely can find three homes exactly like subject property
 Must make adjustments to account for differences in:
 - Time
 - Location
 - Physical characteristics
 - Terms of sale
- The more adjustments, the less reliable the comparable as an estimate of value

Replacement Cost Method

- "Replacement cost method" is based on premise that a property's value won't exceed cost of replacing it
 - Step 1: Estimate cost of replacing building and any other improvements on property
 - Step 2: Estimate and deduct any accrued depreciation
 - Step 3: Add value of lot to depreciated value of improvements

Estimating Replacement Cost

- Replacement cost
 - How much it would currently cost to construct a new building with equivalent utility
- Reproduction cost
 - How much it would cost to construct an exact replica of the building, at current prices
- "Square foot method" is simplest way to estimate replacement cost
 - Analyze cost per square foot for recently built comparables
 - Multiply estimated cost per square foot by number of square feet of subject
 - Make appropriate adjustments
- Example:
 Subject property is a ranch-style home
 1800 sq ft
 Analysis of construction cost of 3 recently built home of comparable size – estimate is \$126.37/sq ft
 $1800 \text{ sq ft} \times \$126.37/\text{sq ft} =$
 \$227,466 estimated cost of replacing improvements

Estimating Depreciation

- Depreciation = loss in value from any cause
- Value can be lost because of:
 - Deferred maintenance
 - Functional obsolescence
 - External obsolescence
- Deferred maintenance
 - Physical wear and tear, damage, and structural defects that reduce the value of the property
 - Also called physical depreciation
- Functional obsolescence
 - Loss in value due to inadequacies such as poor design or outmoded features
 - Also called functional depreciation
- External obsolescence
 - Loss in value due to factors outside the property, such as deteriorating neighborhood, zoning changes, or poor access to schools, shopping or employment centers
- Depreciation is either:
 - Curable (cost of correcting recoverable), or
 - Incurable (cost of correcting not recoverable)
- Example:
\$227,466 est. replacement cost
MINUS
\$8,510 deferred maintenance (roof needs repair, garage door needs replacing)
MINUS
\$7,050 functional obsolescence (living room is too small, family room too far from kitchen)
MINUS
\$3,000 external obsolescence (odors from nearby factory)
EQUALS
\$208,906 Depreciated value of improvements
- Appraisal is submitted to underwriter in one of two ways:
 - "As is"
 - "Subject to"
- "As is" appraisal reports deferred maintenance, but final value estimate is market value of property in its current condition
- "Subject to" appraisal's value estimate represents what market value would be if deferred maintenance were corrected

Adding Land Value

- Last step in replacement cost method is adding value of land to depreciated value of improvements
- Land value estimated by sales comparison method
- Example:
\$208,906 depreciated value of improvements
-PLUS-
\$59,000 land value
-EQUALS-
\$267,906 depreciated value of property

Income Method

- Income method - is based on idea that relationship exists between income a property generates and its value
- Since residential property isn't generally income-producing, appraisers use "gross multiplier" method to estimate value
- In gross multiplier method, appraiser looks at relationship between rental property's income and price paid for property
 - Gross rent multiplier (GRM) = Sales price ÷ Monthly rental income
 - Gross income multiplier (GIM) = Sales price ÷ Annual rental income
- Appraiser locates at least 4 comparables and determines a multiplier
- Example:

Comp	Sales Price	Mo. Rent	Mo. Multiplier
1	\$237,500	\$1,950	\$121.79
2	\$245,000	\$1,975	\$124.05
3	\$250,000	\$2,025	\$123.46
4	\$253,500	\$2,100	\$120.71

- After adjusting multipliers to account for differences, appraiser multiplies rent generated by subject property to find value of property
- Several types of rent appraiser can use to measure the subject property's value:
 - Economic rent - rent the property could generate in current marketplace if it were available
 - Contract rent - rent owner is actually receiving

Final Value Estimate

- After applying three appraisal methods, appraiser must analyze results to find value of property
- Reconciliation - the process of analyzing and comparing appraisal results to draw a conclusion about property's value
 - Not an average of the three numbers
 - Appraiser weighs results for reliability
 - Sales comparison method most important for residential property

Dealing with Low Appraisals

- Uniform Residential Appraisal Report form is used for nearly all residential loan transactions
 - Breaks down appraisal information into logical format
 - Great reference when confronted with a low appraisal

- Low appraisal

- An estimate of value that is below the price agreed upon by the buyer and seller
 - If sale contingent on financing, buyer may not have to complete the sale
 - Low appraisal means smaller loan and bigger down payment

- Example:

Buyer's prepared to make a 10% d/p for a 90% loan

Sales price is \$300,000

Appraised value is \$291,000

Max loan is 90% of \$291,000

\$291,000 a/v x 90% LTV = \$261,900 max l/a

Because the low appraisal (\$9,000 less than p/p) the l/a is limited to \$261,900. Buyer was expecting to make a \$30,000 d/p (\$300,000 p/p x 90% LTV = \$270,000 l/a) But the buyer will now have to make a \$38,100 d/p (\$300,000 - \$261,900 = \$38,100) to pay the \$300,000 price

Possible solutions after low appraisal:

- Buyer pays over value
- Seller lowers price to appraised value
- Compromise price
- Request for reconsideration of value

Some real estate agents will request a copy of the appraisal; it must come from the homeowner to the real estate agent.

Uniform Residential Appraisal Report										File #	
The purpose of this summary appraisal report is to provide the lender/client with an accurate, and adequately supported, opinion of the market value of the subject property.											
Property Address			City			State			Zip Code		
Borrower			Owner of Public Record			County					
Legal Description											
Assessor's Parcel #			Tax Year			R.E. Taxes \$					
Neighborhood Name			Map Reference			Census Tract					
Occupant <input type="checkbox"/> Owner <input type="checkbox"/> Tenant <input type="checkbox"/> Vacant			Special Assessments \$			<input type="checkbox"/> PUD <input type="checkbox"/> HOA \$			<input type="checkbox"/> per year <input type="checkbox"/> per month		
Property Rights Appraised <input type="checkbox"/> Fee Simple <input type="checkbox"/> Leasehold <input type="checkbox"/> Other (describe)											
Assignment Type <input type="checkbox"/> Purchase Transaction <input type="checkbox"/> Refinance Transaction <input type="checkbox"/> Other (describe)											
Lender/Client			Address								
Is the subject property currently offered for sale or has it been offered for sale in the twelve months prior to the effective date of this appraisal? <input type="checkbox"/> Yes <input type="checkbox"/> No											
Report data source(s) used, offering price(s), and date(s).											
I <input type="checkbox"/> did <input type="checkbox"/> did not analyze the contract for sale for the subject purchase transaction. Explain the results of the analysis of the contract for sale or why the analysis was not performed.											
Contract Price \$			Date of Contract			Is the property seller the owner of public record? <input type="checkbox"/> Yes <input type="checkbox"/> No			Data Source(s)		
Is there any financial assistance (loan charges, sale concessions, gift or downpayment assistance, etc.) to be paid by any party on behalf of the borrower? <input type="checkbox"/> Yes <input type="checkbox"/> No											
If Yes, report the total dollar amount and describe the items to be paid.											
Note: Race and the racial composition of the neighborhood are not appraisal factors.											
Neighborhood Characteristics				One-Unit Housing Trends				One-Unit Housing		Present Land Use %	
Location <input type="checkbox"/> Urban <input type="checkbox"/> Suburban <input type="checkbox"/> Rural				Property Values <input type="checkbox"/> Increasing <input type="checkbox"/> Stable <input type="checkbox"/> Declining				PRICE AGE		One-Unit %	
Built-Up <input type="checkbox"/> Over 75% <input type="checkbox"/> 25-75% <input type="checkbox"/> Under 25%				Demand/Supply <input type="checkbox"/> Shortage <input type="checkbox"/> In Balance <input type="checkbox"/> Over Supply				\$ (000) (yrs)		2-4 Unit %	
Growth <input type="checkbox"/> Rapid <input type="checkbox"/> Stable <input type="checkbox"/> Slow				Marketing Time <input type="checkbox"/> Under 3 mths <input type="checkbox"/> 3-6 mths <input type="checkbox"/> Over 6 mths				Low		Multi-Family %	
Neighborhood Boundaries								High		Commercial %	
								Pred.		Other %	
Neighborhood Description											
Market Conditions (including support for the above conclusions)											
Dimensions Area Shape View											
Specific Zoning Classification Zoning Description											
Zoning Compliance <input type="checkbox"/> Legal <input type="checkbox"/> Legal Nonconforming (Grandfathered Use) <input type="checkbox"/> No Zoning <input type="checkbox"/> Illegal (describe)											
Is the highest and best use of the subject property as improved (or as proposed per plans and specifications) the present use? <input type="checkbox"/> Yes <input type="checkbox"/> No If No, describe											
Utilities Public Other (describe)			Public Other (describe)			Off-site Improvements—Type			Public Private		
Electricity <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>			Water <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>			Street			<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		
Gas <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>			Sanitary Sewer <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>			Alley			<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		
FEMA Special Flood Hazard Area <input type="checkbox"/> Yes <input type="checkbox"/> No			FEMA Flood Zone			FEMA Map #			FEMA Map Date		
Are the utilities and off-site improvements typical for the market area? <input type="checkbox"/> Yes <input type="checkbox"/> No If No, describe											
Are there any adverse site conditions or external factors (easements, encroachments, environmental conditions, land uses, etc.)? <input type="checkbox"/> Yes <input type="checkbox"/> No If Yes, describe											
General Description Foundation Exterior Description materials/condition Interior materials/condition											
Units <input type="checkbox"/> One <input type="checkbox"/> One with Accessory Unit		<input type="checkbox"/> Concrete Slab <input type="checkbox"/> Crawl Space		Foundation Walls		Floors					
# of Stories		<input type="checkbox"/> Full Basement <input type="checkbox"/> Partial Basement		Exterior Walls		Walls					
Type <input type="checkbox"/> Det. <input type="checkbox"/> Att. <input type="checkbox"/> S-Det./End Unit		Basement Area sq. ft.		Roof Surface		Trim/Finish					
<input type="checkbox"/> Existing <input type="checkbox"/> Proposed <input type="checkbox"/> Under Const.		Basement Finish		% Gutters & Downspouts		Bath Floor					
Design (Style)		<input type="checkbox"/> Outside Entry/Exit <input type="checkbox"/> Sump Pump		Window Type		Bath Wainscot					
Year Built		Evidence of <input type="checkbox"/> Infestation		Storm Sash/Insulated		Car Storage <input type="checkbox"/> None					
Effective Age (Yrs)		<input type="checkbox"/> Dampness <input type="checkbox"/> Settlement		Screens		<input type="checkbox"/> Driveway # of Cars					
Attic <input type="checkbox"/> None		Heating <input type="checkbox"/> FWA <input type="checkbox"/> HWBB <input type="checkbox"/> Radiant		Amenities <input type="checkbox"/> Woodstove(s) #		Driveway Surface					
<input type="checkbox"/> Drop Stair <input type="checkbox"/> Stairs		<input type="checkbox"/> Other <input type="checkbox"/> Fuel		<input type="checkbox"/> Fireplace(s) # <input type="checkbox"/> Fence		<input type="checkbox"/> Garage # of Cars					
<input type="checkbox"/> Floor <input type="checkbox"/> Scuttle		Cooling <input type="checkbox"/> Central Air Conditioning		<input type="checkbox"/> Patio/Deck <input type="checkbox"/> Porch		<input type="checkbox"/> Carport # of Cars					
<input type="checkbox"/> Finished <input type="checkbox"/> Heated		<input type="checkbox"/> Individual <input type="checkbox"/> Other		<input type="checkbox"/> Pool <input type="checkbox"/> Other		<input type="checkbox"/> Att. <input type="checkbox"/> Det. <input type="checkbox"/> Built-in					
Appliances <input type="checkbox"/> Refrigerator <input type="checkbox"/> Range/Oven <input type="checkbox"/> Dishwasher <input type="checkbox"/> Disposal <input type="checkbox"/> Microwave <input type="checkbox"/> Washer/Dryer <input type="checkbox"/> Other (describe)											
Finished area above grade contains: Rooms Bedrooms Bath(s) Square Feet of Gross Living Area Above Grade											
Additional features (special energy efficient items, etc.)											
Describe the condition of the property (including needed repairs, deterioration, renovations, remodeling, etc.).											
Are there any physical deficiencies or adverse conditions that affect the livability, soundness, or structural integrity of the property? <input type="checkbox"/> Yes <input type="checkbox"/> No If Yes, describe											
Does the property generally conform to the neighborhood (functional utility, style, condition, use, construction, etc.)? <input type="checkbox"/> Yes <input type="checkbox"/> No If No, describe											

Regulation Z - Appraisers and Appraisals

The following section will review the special rules under Regulation Z for appraisals

Appraisals - Valuation Independence

Regulation Z 1026.42 Subpart E - Special Rules for Certain Home Mortgage Transactions

Appraiser independent requirements are designed to ensure the integrity of real estate appraisals and apply to all consumer credit transactions secured by a principal dwelling, including home equity lines of credit.

Requirements under Regulation Z

The following requirements were imposed to ensure the integrity of real estate appraisals: (This is a summary of the rule; excerpts from the law will follow)

- Person performing valuations can only be based the appraised value on factors using their independent judgment
 - Prohibits coercion of any type
- Prohibits those involved in performing valuations, along with valuation companies, from having a financial - or other interests - in the property or the transaction itself
- Creditors cannot extend credit if it is known that coercion has taken place or a conflict of interest
 - Unless the value of the property is not materially misstated or misrepresented
- Creditors or settlement service providers must file reports about appraiser wrongdoing
- Appraisers must be paid reasonable and customary compensation
 - Cannot be employees of the creditor of the appraisal management company hired by the creditor

Sections of the law

The following information is taken directly from this section of the Truth in Lending Act, Reg Z

Scope 1026.42(a). This section involves open and closed end transactions secured by the consumer's principal dwelling

Definitions 1026.42(b)

- Covered persons 1026.42(b)(1) - will include:
 - Creditors, mortgage brokers, appraisal managements companies, real estate agents appraisers
 - Anyone who provides settlement services
- Those who would not be covered :
 - The consumer obtaining credit via a covered transaction
 - A guarantor
 - A non-obligor spouse

Valuation 1026.42 (b)(2)(i)(ii)(iii)

- Estimate of value of the consumer's principal dwelling
 - Can be written or electronic form
 - Includes photos and other information
 - Prepared by a natural person
 - Such as an appraiser
 - Realtor can perform estimate of market value
 - Estimate is a range of values for the property

Coercion 1026.42 (c)(1)

- No covered person defined in 1026.42(b)(1) above can directly or indirectly cause the value given by the appraiser to be based on factors other than the independent judgment of the appraiser through:
 - Coercion
 - Extortion
 - Inducement
 - Bribery
 - Intimidation
- Examples of Coercion 1026.42(c)(1)(i)(A)(B)(C)(D)
 - Influence the appraiser to give a value of minimum or maximum value
 - Threatening to, or actually withholding payment to the appraiser because they disagree with the appraised value
 - Implying to an appraiser that future business is dependent upon a certain estimate of value
 - Not including appraiser for future work because an appraised value did not meet their appraised value amount needed for the transaction
 - Making compensation paid a condition upon the loan actually closing

Mischaracterization of Value 1026.42(c)(2)(i)(ii)(iii)

- Those preparing appraisal will not misrepresent the value of a property
 - A bona fide error is not considered misrepresentation
 - No one is allowed to falsify or alter a valuation
 - Except for the person preparing the valuation can make alterations
 - Inducing a person to violate this section will not be allowed
- Permitted actions will include 1026.42(c)(3)(i)(ii)(iii)(iv)(v)(vi)
 - Appraiser can be asked to consider
 - Additional comparables
 - Property information
 - Providing additional details, substantiation, or to explain the reason for the value
 - Correcting errors in the report
 - Obtaining multiple valuations
 - Compensation can be withheld if there is a breach of contract or poor quality of services rendered
 - Action can be taken if it is permitted or required by Federal or state laws or agency guidance

Prohibition on Conflicts of Interest 1026.42 (d)(1)(i)(ii)(A)(B)

- The person preparing a valuation report may not have a direct or indirect interest in the property or the transaction itself
 - This includes a financial interest or otherwise
 - Prohibited interest in the transaction includes
 - Loan officer of the creditor
 - Mortgage broker
 - Real estate broker
 - Any other settlement service provider
 - Any person compensated or who receives financial or other benefits based on the transaction being consummated
- Employees and Affiliates of Creditors; Providers of Multiple Settlement Services
 - A creditor is not in violation of this section based solely on the fact that the preparer of the valuation is an employee or affiliate of the creditor, or
 - A person provides a settlement service in addition to preparing valuations or valuation management functions
- Employees and Affiliates of Creditors with Assets of More than \$250 for Both of the Past Two Calendar Years 1026.42(2)(i)(ii)
 - The appraiser's compensation is not based on the value of the appraisal
 - The employee, officer or director involved in the loan production function will not partake in the decision to approve, deny, or set the terms of the transaction
- Employees and Affiliates of Creditors with Assets of \$250 or less for Either of the Past Two Calendar Years 1026.42(3)(i)(ii)
 - The appraiser's compensation is not based on the value of the appraisal

- The involved in performing the valuation or any valuation management functions, is not part of the creditor's loan production function
- And does not report to someone whose payment is based on the consummation of the loan
- The employee, officer or director involved in the loan production function will not partake in the decision to select, retain, recommend or influence the appraiser

Definitions - In Regards to Paragraph (d) - 1025.42 (5)(I)(ii)(iii)

- Loan Production Function - Will mean an employee, officer, director, department, division, or other person responsible for producing or approving covered transactions
- Settlement Service --(same as RESPA, 12 U.S.C. 2601) "Includes any service provided in connection with a real estate settlement including, but not limited to, the following: title searches, title examinations, the provision of title certificates, title insurance, services rendered by an attorney, the preparation of documents, property surveys, the rendering of credit reports or appraisals, pest and fungus inspections, services rendered by a real estate agent or broker, the origination of a federally related mortgage loan (including, but not limited to, the taking of loan applications, loan processing, and the underwriting and funding of loans), and the handling of the processing, and closing or settlement"
- Affiliate - same as Regulation Y, Board of Governors of the Federal Reserve System, 12 CFR 225.2(a)) - "Any company that controls, is controlled by, or is under common control with, another company"

When Extension of Credit Prohibited - 1026.42 (e)

- If the creditor is aware of a violation, either before or at the closing of a transaction, they are prohibited from extending credit
- Unless the creditor is aware the violation does not materially misrepresent or misstate the value of the property

Customary and Reasonable Compensation- 1026.42 (f)(1)(2)(i)(A-F)

- Compensation provided to fee appraisers must be fair and reasonable, comparable to amounts paid to similar appraisal services
- The following factors will be used to show compensation is reasonable:
 - Type of property
 - Scope of work
 - Time appraisal services are completed
 - Qualifications of fee appraiser
 - Work quality, experience and professional record of fee appraiser
 - Quality of work
- Definitions - Regarding Paragraph (f) - 1026.42(i)(A)(b)(ii)(iii)(A-D)
 - Fee Appraiser - A person who is state-licensed or state-certified and receives a fee to perform an appraisal
 - Is not an employee of the person requesting the appraisal
 - An organization that employs state-licensed or state-certified appraisers, receives a fee for performing appraisals
 - Appraisal Services - Services required to perform an appraisal, includes
 - Defining scope of work
 - Inspection of the property
 - Review of any necessary public and private data sources
 - Examples: Multiple Listing Service, tax and public land records
 - Appraisal Management Company - A person authorized to perform one or more of the following:
 - Recruit, select, and retain fee appraisers
 - Contract with fee appraisers
 - Manage the entire process of the appraisal
 - Review and verify appraiser's work

Mandatory Reporting 126.42 (g)(1)(2)(3)

- If the Uniform Standards of Professional Appraisal Practice (USPAP), or the rules of state or federal laws have been violated, any covered person will report the violation to the proper authorities

- Notification to the property authority should be within a reasonable time frame once a violation has been discovered
- State agency "state appraiser certifying and licensing agency"
 - An appropriate state agency is the agency in which the consumer's principal dwelling is located

FannieMae has on its website, fanniemae.com, the following information regarding appraisers:

Fannie Mae's lender partners rely on appraisers to provide them with thorough, accurate, and objective appraisal reports that result in reliable opinions of market value so they can make prudent underwriting decisions. The appraisal is used to judge the property's acceptability for the mortgage loan requested in view of its value and marketability.

FHA LOANS

Upon completion of this lesson, you should be able to:

- Understand FHA's different programs
- Comprehend graduated payment mortgages
- Compute FHA insurance premiums
- Know about sales concessions such as seller contributions
- Understand secondary financing and FHA loans
- Become familiar with the assumption rules for FHA loans

FHA

- Two federal home financing programs:
 - FHA-insured loan program
 - VA-guaranteed loan program
- Federal Housing Administration (FHA) was created in 1934 as part of National Housing Act
 - Purpose of act:
 - To generate new jobs by increasing construction activity
 - Stabilize mortgage market
 - Promote financing, repair, improvement, and sale of real estate
- Today, FHA is part of Department of Housing and Urban Development (HUD)
- Primary function is insuring mortgage loans
- Compensates lenders for losses from borrower default
- Does not build homes or make loans
- Mutual Mortgage Insurance Plan is FHA insurance program funded by premiums paid by FHA borrowers
- Direct endorsers - lenders authorized to handle entire underwriting process for FHA loans
- If FHA borrower defaults on loan:
 - FHA reimburses lender for full amount of loss
 - Borrower required to repay FHA

Characteristics of FHA Loans

- Typical FHA loan has a 30-year term, but borrower may have option for shorter term. Other characteristics of an FHA loan:
 - Required to have first lien position
 - Competitive interest rates
 - Lender charges an origination fee and may charge discount points
 - Borrowers may use gift funds
- Distinguishing features of FHA loans, almost every FHA-insured loan has these characteristics:
 - Less stringent qualifying standards.
 - Borrowers with minimum decision credit score at or above 580 are eligible for maximum financing
 - 3.5% down payment

- Borrowers with minimum credit score between 500 and 579 – limited to 90% LTV
- Borrowers with minimum credit score of less than 500 are not eligible for FHA-insured mortgage financing
 - Secondary financing restrictions
 - Maximum loan amounts set by local limits and by LTV rules
 - Borrower must come up with minimum cash investment plus funds for
 - Closing costs
 - Discount points
 - Prepaids
 - Mortgage insurance is required for the life of the loan
 - No pre-payment charges
 - Property must be owner-occupied primary residence

FHA Loan Programs

FHA has many different programs to fit different needs. Each is funded annually on a national basis

- These programs are of the greatest interest to home buyers:
 - Section 203(b) – fixed-rate mortgages on owner-occupied residences with up to four units
 - Borrower must meet standard FHA credit qualifications
 - Borrower is eligible for approx. 96.5% financing
 - Borrower is able to finance the upfront MIP
 - Also responsible for paying an annual premium
 - UPFMI: When buyers are approved for FHA home loans, they are required to carry mortgage insurance. That includes both a Mortgage Insurance Premium (MIP) and an Up Front Mortgage Insurance Payment (UFMIP). The Upfront Mortgage Insurance Premium payments go into an escrow account set up by the U.S. Treasury Department and the funds are used to protect the government in case the borrower defaults on the FHA loan.
 - Eligible properties are 1 – 4 units
 - Section 203(k) – mortgages used to purchase/refinance and rehabilitate a residence with up to four units
 - Section 223(e) – loans in older, declining urban areas
 - Section 234(c) – loans on owner-occupied condominium units
 - Section 245 and Section 245(a) – graduated payment mortgages and growing equity mortgages
 - Section 251 – adjustable-rate mortgages
 - Owner-Occupancy Requirement
 - Borrowers must intend to occupy property
 - Must be the borrower's principal residence
 - If more than one unit, borrower must use one as principal residence
 - Secondary Residences
 - This is a home borrower occupies less than 50% of the time
 - Can be financed only if denial would cause hardship
 - Must be need for employment-related reasons
 - Cannot be a vacation home
 - Investor Loans
 - FHA generally does not insure investor homes
 - Exception may be made for investor who wants to purchase a property that HUD owns thru foreclosure
- Most FHA loans are 203(b) loans
- Program can be used for purchase loans or refinancing for residences with up to four units
- HUD imposes limits on size of loans that can be insured
- Two different limits:
 - Local loan amount limits
 - Loan-to-value ratio limits
- Local maximum loan amounts
 - FHA max loan amounts based on local median house prices
 - Vary from one area to another
 - Each has local max for 1, 2 3 & 4 units
 - FHA maximum loan amounts are tied to the conforming loan limits
 - Set annually by the secondary market agencies
 - Subject to annual adjustments

- Currently FHA max is set at 65% of Freddie Mac's general conforming loan limit
- One unit – Freddie Mac current loan limit for 2016 is \$417,000
- Therefore, FHA's basic max l/a for a one unit for 2016 is \$271,050
 $\$417,000 \times .65 = \$271,050$
- Instead of one national mortgage limit like Fannie Mae, loan limits will depend on whether a property is in a general or high-cost area
- Each year, FHA recalculates its loan limits based on 115 % of the median house price in the area. For counties, or equivalent, located in Metropolitan Statistical Areas (MSAs) the limit for all areas in the MSA is calculated based on the highest cost county.
- There is no change to the FHA national loan limit "ceiling" which remains at \$625,500 and the "floor" which remains at \$271,050. FHA's minimum national loan limit "floor" is set at 65 percent of the national conforming loan limit of \$417,000. The floor applies to those areas where 115 percent of the median home price is less than 65 percent of the national conforming loan limit.
- Any area where the loan limit exceeds the "floor" is considered a high cost area. The maximum FHA loan limit "ceiling" for high cost areas is 150 percent of the national conforming limit.
- Additional information and loan limit adjustments for two-, three-, and four-unit properties, and in Special Exception Areas, are noted in FHA's mortgagee letter. An attachment to the Mortgagee Letter provides
- Local loan amount limits - HUD often sets loan amounts on county-by-county basis
 - In county with large city, entire county may be treated as high-cost area
 - Housing is more expensive than average
 - FHA may increase the max l/a to 125% of area median house price

2016 FHA Maximum Loan Amounts		
Number of Units	Basic Maximum Loan Amounts	Maximum Loan Amount in High Cost Areas †
1	\$271,050	115% of median price, up to \$625,500
2	\$347,000	115% of median price, up to \$800,775
3	\$419,425	115% of median price, up to \$967,950
4	\$521,250	115% of median price, up to \$1,202,925
† In Alaska, Hawaii, Guam, and the Virgin Islands, the 2016 ceilings are \$938,250 for one unit; \$1,201,150 for two units, \$1,451,925 for three units; and \$1,804,375 for four units.		

Minimum Cash Investment & LTV

- Borrower must make minimum cash investment of at least 3.5% of appraised value or sales price, lesser of two
- Max LTV on FHA loan is 96.5%
- Closing costs paid by borrower no longer count towards min cash investment
 - Also not included:
 - Discount points
 - Prepaid expenses
 - Borrower must come up with min cash investment plus funds for:
 - Closing costs
 - Discount points
 - Prepays
 - Borrower not allowed to use secondary financing from seller or lender for min cash investment
 - Can use funds provided by family member

Sales Concessions

- FHA places certain restrictions on sales concessions
- Purpose is to prevent parties from using contributions to defeat FHA's loan-to-value rules

Seller Contributions

- FHA considers it to be a seller contribution if seller (or other interested party) pays for all or part of:
 - Buyer's closing costs
 - Buyer's prepaid expenses
 - Any discount points
 - Temporary or permanent buydown
 - Buyer's mortgage interest
 - Upfront MIP
- Seller contributions are limited to 6% of sales price
- Excess contributions are treated as inducements to purchase
 - Deducted from sales price in loan amount calculations
- 6% limit only applies to contributions paid for by seller or another interested party
- Example:

The Johnson's are buying a home for \$254,000 and financing the purchase with an FHA loan. The seller has agreed to pay the lender \$16,000 to buy down the interest rate on the Johnson's loan. Six percent of the sales price is \$15,240, so the buydown is \$760 over the 6% limit on seller contributions (\$16,000 - \$15,240 = \$760). The \$760 excess seller contribution will be treated as an inducement to purchase.

Inducements to Purchase

- FHA considers it to be an inducement to purchase if seller (or other interested party):
 - Gives buyer a decorating allowance
 - Gives buyer a repair allowance
 - Pays for buyer's moving expenses
 - Pay real estate agent's sales commission on sale of buyer's current home
 - Pays the buyer's agent a larger sales commission than is customary in the local area
 - Gives buyer personal property not customarily included in sale of home
- Value of inducements are subtracted from property's sale price before LTV ratio is applied
 - Reduces amount of mortgage available to FHA borrower
- Example:

Returning to the previous example, suppose that the seller has also agreed to give the Johanssons \$1,000 towards their moving costs. This \$1,000 and the \$760 excess in seller contributions are considered inducements to purchase, and they're subtracted from the property's sales price before the maximum loan amount is calculated.

\$ 254,000	Sales Price
- 1,760	Inducements to Purchase
\$ 252,240	Adjusted Sales Price
x .965	Maximum Loan-to-Value Ratio (96.5%)
\$ 243,411	Maximum Loan Amount

Secondary Financing

- FHA rules regarding use of secondary financing depend on whether financing is being used for minimum cash investment or as supplement to make up permitted base loan amount

Cash Investment

- Generally, borrower not allowed to use secondary financing from seller, another interested party, or institutional lender to pay:
 - Minimum cash investment
 - Closing costs
 - Other expenses
- If secondary financing is a family member, total financing can't exceed property's value or sales price plus closing costs, prepaids, and discount points
 - Combined payments can't exceed buyer's ability to pay
- FHA borrower who is 60 years or older may borrow money from:
 - Relative
 - Close friend with clearly defined interest in borrower
 - Employer
 - Charitable organization
- Same value requirements as with family and agencies

Base Loan

- FHA allows second mortgages from anyone with FHA-insured loan. Following conditions must be met:
 - Both loans together can't exceed FHA maximum mortgage amount
 - Combined total of payments may not exceed borrower's ability to pay
 - If second loan has periodic installment payments, they must be collected on a monthly basis. Payment amounts should be substantially the same
 - Second mortgage may not have balloon payment due less than 10 years after closing
 - Second mortgage may not impose prepayment penalty

Assumption of FHA Loans

- FHA loans closed before December 15, 1989 can be assumed:
 - By any buyer
 - Without FHA or lender approval
 - By an investor (non-occupant)
- For FHA loans closed after December 15, 1989, buyer assuming loan must:
 - Pass creditworthiness review
 - Occupy home
- For FHA loans closed on or after January 27, 1991, home must be buyer's primary residence
 - May not be a second home
- For FHA loans closed between February 5, 1988 and January 27, 1991, if:
 - Original borrower was owner occupant
 - Buyer is purchasing property as a second home
 - Then loan must be paid down to 85% LTV ratio

Assumption Charges

- Interest rate on fixed-rate FHA-insured loan normally isn't raised after assumption
 - Lender allowed to charge \$500 assumption fee if loan originated after December 15, 1989

FHA Underwriting

- FHA underwriting standards aren't as strict as Fannie Mae/Freddie Mac standards
 - Involves analysis of applicant's income, net worth, and credit history

Income Analysis

- FHA underwriter determines applicant's monthly effective income
- Effective income - gross income from all sources expected to continue for first 3 years of loan term
- Underwriter also applies income ratios to determine adequacy of effective income:
 - Fixed payment to income ratio (generally 43%)
 - Housing expense to income ratio (generally 31%)
- Fixed payments include proposed monthly housing expense and all recurring charges
- Housing expense:
 - Principal and interest
 - Property taxes
 - Hazard insurance
 - One-twelfth of FHA annual premium
 - Any homeowners' dues
 - Flood insurance or additional insurances
- Recurring charges:
 - Monthly payments on debt with 10 or more remaining payments
 - Alimony and child support payments
 - Installment debt payments
 - Payments on revolving credit accounts
 - Calculating Recurring Charges – Example

Helen Crowder wants to buy a home using FHA financing. In the area where she lives, the maximum FHA loan amount is \$271,050 and lenders are generally charging about 5.5% interest for 30-year fixed rate FHA loans. She'd like to get preapproved for the maximum loan amount. The monthly payment (including principal, interest, taxes, hazard insurance, and mortgage insurance) for a loan that size would be approximately \$1,693. Crowder's monthly salary is \$4,500. Her ex-husband reliably sends her a child support payment each month for their four-year-old daughter. The child support is tax-exempt, so the lender "grosses up" the payment, and concludes that it's the equivalent of \$650 in taxable income. Thus, Crowder's effective income is \$5,150.

Crowder has to pay the following recurring charges every month:

\$ 253	Car Payment (11 payments remaining)
65	Furniture store payment (15 payments remaining)
55	Minimum Visa payment
29	Minimum MasterCard payment
125	Student loan (63 payments remaining)
+ 60	<u>Average payment on Texaco credit card</u>
\$587	Total Recurring Charges

Calculating Debt to Income Ratio Example

To calculate Crowder's debt to income ratio, first add the proposed housing expense to her recurring charges to determine her total fixed payments. Then divide that figure by her effective income.

\$1,693	Proposed housing expense
+ 587	Recurring charges
<hr/>	
\$2,280	Total Fixed Payments
<u>\$ 2,280</u>	Total Fixed Payments
<hr/>	
5,150 (÷)	Effective income
0.4427	Debt to Income Ratio (44%)

With the \$1,693 proposed monthly payment, Crowder's housing expense to income ratio would be approximately 33%:

\$ 1,693	Proposed housing expense
<hr/>	
5,150 (÷)	Effective income
0.3287	Housing expense to income ratio (33%)

- If income ratios exceed 43% and/or 31% limits, applicant won't qualify for loan unless there are compensating factors that reduce risk of default
- Compensating factors include:
 - Paid housing expenses at least equal to proposed expenses for last 12-24 months
 - Plans to make large down payment (10%)
 - Demonstrated ability to accumulate savings and conservative attitude toward use of credit
 - Able to devote greater portion of income to housing expenses
 - Receives income not counted as effective income, but directly affects ability to pay
 - Proposed housing expense only a small increase (10% or less) of current housing expense
 - Will have substantial reserves after closing (at least 3 mortgage payments)
 - Job training or professional education indicate potential for increased earnings
- If home is an energy-efficient home, income ratios can be exceeded by 2%
- Temporary buydowns are allowed if buyer qualifies at note rate
 - So if buydown brings interest rate down from 9% to 7%, buyer must qualify for loan at 9%

Assets for Closing

- At closing, borrower needs enough cash to cover:
 - Minimum cash investment
 - Prepaids
 - Any discount points
 - Upfront MIP (if not financed)
 - Any closing costs, repair costs, or other expenses not financed
- Generally, borrower not required to have reserves for FHA loan
 - But reserves may be a compensating factor if income ratios exceed limits
- May also borrow money required for closing from someone other than relative, if loan is secured by collateral other than home being purchased

Other Closing Requirements

- FHA has several requirements related to inspection of properties used to secure FHA-insured loans
- First, buyers must receive HUD-provided disclosure form titled “For Your Protection: Get a Home Inspection”
 - Explains importance of home inspections
 - Distinguishes them from appraisals
- By signing form, buyers acknowledge that FHA will not perform home inspection or guarantee property’s price or condition
- Second, buyers must receive disclosure form titled “Notice to the Homebuyer”
 - Summarizes conditions noted by FHA-approved appraiser preventing approval of property
 - Part of disclosure package
 - Must be disclosed within 3 days of loan application

FHA Insurance Premiums

- Insurance premiums for FHA loans are either:
- MMI (mutual mortgage insurance premiums)
- MIP (mortgage insurance premiums)
- For most programs, borrowers pay an upfront premium and annual premiums

Upfront MIP

- Upfront premium (UFMIP) is also called “one-time premium” (OTMIP)
- Paid in cash, or financed
- Percentage of base loan amount (currently 1.75%)
- Example: John Rubino is buying a house with a \$350,280 FHA loan. His upfront premium will be \$3,520.80.

\$ 350,280	Loan Amount
x 1.75%	Premium Percentage
<hr/>	
\$6,129.90	UFMIP

- Either borrower or seller can pay UFMIP in cash at closing
- May also be financed over loan term
 - Added to base loan amount
- Borrower can borrow maximum loan amount plus UFMIP
 - Example: Rubino has chosen to finance his upfront MIP instead of paying it in cash at closing.

\$ 350,280.00	Loan Amount
+ 6,129.90	UFMIP
<hr/>	
\$ 356,409.90	Total Amount Financed

- Loan origination fee is based only on base loan amount, not including UFMIP
 - Example: 1% origination with l/a @ \$350,280
 $\$350,280 \times .01 = \$3,502.80$
- Discount points are based on total amount financed, including upfront MIP
 - Example: 1% discount with a l/a @ \$350,280 plus \$3,520.80 (UFMIP) = \$353,782.80
 $\$353,782.80 \times .01 = \$3,573.83$
- FHA buyer may be entitled to refund of part of UFMIP if loan is paid off early
 - FHA “earns” premium under a schedule

- Borrower gets refund whether UFMIP was paid in cash or financed
- But borrower not entitled to refund if:
 - Selling property and allowing buyer to assume FHA loan
 - Loan made after December 8, 2004 (unless loan is to refinance another FHA loan)

Annual Premiums

- Exceptions: 15 year term with an LTV of 78% or less

Most FHA buyers are required to pay annual renewal premiums in addition to UFMIP. Annual premiums will be a percentage of the loan balance.

- 15-year loan term
 - LTV less than or equal to 78 percent - 0.45% annually
 - LTV greater than 78 percent, less than 90 percent - 0.45% annually
 - LTV greater than 90 percent - 0.70% annually
- 30-year loan term
 - LTV less than or equal to 95 percent: 1.30% annually
 - LTV greater than 95 percent - 1.35% annually

Annual MIP Chart

LTV Ratio	Annual Premium for over 15 Years and up to 30 Years	LTV Ratio	Annual Premium for Loans 15 Years and Under
95.00% and Under	1.30%	78% and under	0.45%
95.01% and Over	1.35%	90.00% to 78.01%	0.45%
		90.01% and Over	0.70

Note: FHA mortgages for which the loan size exceeds \$625,500 are subject to additional MIP.

Annual Premium Cancellation

FHA will remove annual MIP after 11 years for homeowners whose beginning LTV is 90% or less. For everyone else, including those making a 3.5% down payment, the FHA will charge MIP for the remainder of the loan's term.

CANCELLATION OF MIP

TERM	LTV	PREVIOUS FHA GUIDELINES	EFFECTIVE 04/01/13
≤ 15 yrs	≤ 78	No annual MIP	11 years
≤ 15 yrs	> 78 – 90	Cancelled at 78% LTV	11 years
≤ 15 yrs	> 90	Cancelled at 78% LTV	Loan term
> 15 yrs	≤ 78	5 years	11 years
> 15 yrs	> 78 – 90	Cancelled at 78% LTV & 5 yrs	11 years
> 15 yrs	> 90	Cancelled at 78% LTV & 5 yrs	Loan term

Section 255

- Reverse Mortgage/Home Equity Conversion Mortgage (HECM)
 - Allows older homeowners to convert equity into a monthly source or line of credit
 - Both borrowers must be 62 years or older
 - Borrower must own the property outright or has paid down a considerable amount
 - Borrower cannot be delinquent on any federal debt
 - Borrower must participate in a consumer information session
 - Session will be conducted by a HUD-approved HECM counselor
- Property requirements
 - Single family or 2-4 units
 - if 2-4 units, one unit must be occupied by borrower
 - If condo, must be HUD approved
 - If a manufactured home, must meet FHA requirements
 - Loan amount depends on
 - Lesser of a/v or the GECM FHA loan limit
 - Current interest rates
 - Age of borrower
- Financial requirements
 - Income, assets, monthly expenses and credit history may be verified
 - Also, timely payments of real estate taxes, homeowner's and flood insurance may be verified
 - No repayment as long as property remains the principal residence
 - Closing costs can be financed
- Costs involved with HECM
 - Mortgage insurance premium
 - Guarantees borrower will receive loan advances
 - Can be financed into loan amount
 - Third party charges
 - Can include: appraisal, title search, surveys, recording fees, etc.
 - Origination fee
 - Lender allowed to charge up to \$2,500 if home is valued at less than \$125,000
 - If home is valued at more than \$125,000, lender is allowed to charge 2% of the first \$200,000
 - Plus 1% over the \$200,000 value
 - Servicing Fee
 - Charge by the lender for servicing of the loan
 - Cannot exceed \$30 a month if loan has an annual adjusting rate
 - Cannot exceed \$35 if interest rate adjusts monthly
 - At origination this fee is deducted from loan amount
 - Thereafter, the servicing fee is added to the borrower's loan balance
- Amount borrowed will depend on:
 - Age of the youngest borrower
 - Current interest rate
 - Appraised value or HECM FHA mortgage limit of \$625,500
 - The lesser of the two
 - Initial MIP program
 - HECM Standard
 - HECM Saver
- HECM Standard
 - Mortgage Insurance Premium/MIP
 - 2% of maximum claim amount or appraised value
 - Lesser of the two
 - Plus annual premium thereafter equal to 1.25% of loan balance
- HECM Saver
 - For homeowners who want to borrow a smaller amount
 - Lower proceeds in exchange for lower costs
 - Initial mortgage insurance premium
 - 0.01% of loan amount

- Example: Loan amount =\$100,000
 HECM Saver MIP costs = \$10
 HECM Standard MIP costs = \$2,000
 Annual MIP = 1.25% (Same as HECM Standard)
- MIP guarantees:
 - If loan servicer goes out of business, government will step in and ensure homeowner has access to funds
 - Guarantees homeowner will never owe more than value of home when HECM is repaid
 - Lender recovers amount borrower when property is sold
 - If sale exceeds amount owed, proceeds go to owner
 - If sale is less, FHA will cover
- HECM can be used for purchase
 - 1-4 principal unit
 - Not for second home or investment
 - Example:

The Garcias are empty-nesters who want to downsize from their current home to a nearby condominium. The condo's asking price is \$210,000. They anticipate that they will net \$190,000 from the sale of their current home, but this won't be enough to purchase the new condo outright. The Garcias decide to use an FHA HECM to buy the condo. The HECM loan amount is \$120,000. That amount, plus \$90,000 of their own funds (out of the sale proceeds from their current home), is enough for the condo purchase price (\$120,000 + \$90,000 = \$210,000).

USDA Rural Loans

- Provides homeownership opportunities to rural Americans
 - Includes home renovations
 - Also programs for the elderly, disabled or low-income of multi-unit housing buildings
 - Specific location of property is a possible limitation for the loan
- Highlights of USDA Loans:
 - 100% Financing
 - Broad location guidelines
 - No mortgage insurance requirement
 - No seller contribution limit
 - 100% of closing costs can be gift
 - Loan amount can include closing costs and repairs up to a/v
- Section 502 Loans
 - Helps low-income borrower
 - Purchase in rural areas
 - Must be without adequate housing
 - Able to afford mortgage payments
 - Reasonable credit histories
 - Can be used for:
 - Build
 - Repair
 - Renovate
 - Relocate
 - Home must be modest in:
 - Size
 - Design
 - Cost
 - Manufactured housing must be permanently installed and meet the HUD Manufacturing Housing Construction and Safety Standards and HCFP thermal site standards.
 - Income can be up to 115% median
 - Term
 - 30 years
 - Promissory interest rate set by lender
 - No down payment required
 - House – modest in size, design and cost

- Rural Housing Direct Loans
 - Directly funded by the Government
 - 100% financing
 - Can be used in rural areas to:
 - Purchase existing dwelling
 - Purchase a site and construct a home
 - Purchase new construction
 - Low and very low-income
 - Very low – below 50% of Area Median Income/AMI
 - Low – between 50% - 80% of AMI
 - Moderate – 80% - 100% of AMI
 - Payment subsidy available for repayment
 - Must be unable to obtain credit elsewhere
 - Must have reasonable credit history
- Terms
 - Up to 33 years
 - 38 years w/income below 60% AMI
 - 30 years for manufactured homes
 - Housing must be modest in size, cost, design
 - Modest for the area
 - Market value not in excess of the area
 - No prohibited features
- Rural Housing Repair and Rehab Loans
 - Funded directly by the Government
 - Very low income
 - Must own and occupy property
 - Funds are to:
 - Improve or modernize a home
 - Remove health and safety hazards
- Terms
- 1% interest loan
- Paid over 20 yr period
 - Loans up to \$20,000
 - Grants up to \$7,500

VA LOANS

Upon completion of this lesson, you should be able to:

- Recognize the different characteristics of VA loans
- Understand the eligibility requirements
- Know how the VA guaranty works
- Comprehend the underwriting guidelines for VA loans

Characteristics of VA Loans

- The VA loan program was established to help veterans finance the purchase of their homes. VA offers many advantages over conventional financing
 - VA-guaranteed loans are made by institutional lenders, but a portion of the loan is guaranteed by Department of Veterans Affairs
 - Protects lender against losses from default
 - VA loans may be used to financed purchase or construction of a one to four-unit residences
 - VA Does not guaranty investor loans
 - Veteran must occupy home
 - Key characteristics of VA loans:
 - No down payment required
 - No maximum loan amount
 - No maximum income limits

- Least stringent qualifying standards
- Can be fixed-rate or ARM loans
- No mortgage insurance required
- No maximum interest rate
- Lender may charge flat fee of no more than 1% for administrative costs
- No prepayment penalties
- Forbearance extended to veterans with financial difficulties
- Can be assumed by creditworthy buyer, veteran or non-veteran

Funding Fees

- VA borrowers must pay VA a “funding fee”, instead of paying insurance premiums
 - Amount of funding fee is a percentage of loan amount
- Certain parties are exempt from funding fee requirement:
- Veterans entitled to receive VA compensation for service-related disabilities
- Veterans receiving retirement pay who are entitled to receive disability compensation
- Veterans who are rated by VA as eligible to receive compensation as a result of pre-discharge exam and rating
- Surviving spouses of veterans who died in service or from service-related disabilities

Funding Fees - Purchase and Construction Loans

Type of Veteran	Down Payment	% for First Time Use	% for Subsequent Use
Regular Military	None	2.15%	3.30%
	5% or more (up to 10%)	1.50%	1.50%
	10% or more	1.25%	1.25%
Reserves/ National Guard	None	2.40%	3.30%
	5% or more (up to 10%)	1.75%	1.75%
	10% or more	1.50%	1.50%

Funding Fees - Cash Out Refinances

Type of Veteran	First Time Use	% for Subsequent Use
Regular Military	2.15%	3.30%
Reserves/National Guard	2.40%	3.30%

Eligibility for VA Loans

- Eligibility for VA loans is based on length of continuous active duty service in U.S. armed forces
- 90 days of active duty, between:
 - September 16, 1940 through July 25, 1947 (World War II)
 - June 27, 1950 through January 31, 1955 (Korean War)
 - August 5, 1964 through May 7, 1975 (Vietnam War)
 - August 2, 1990 to present (Persian Gulf War)
- 181 days of active duty during peacetime period:
 - July 26, 1947 through June 26, 1950
 - February 1, 1955 through August 4, 1964
 - May 8, 1975 through September 7, 1980
- For service that began on/after September 8, 1980:
 - 24 months of continuous active duty, or full period of active duty call (at least 181 days)
 - 90 days if during Persian Gulf War
- If veteran applies while still on active duty, he is eligible after serving at least 181 days of continuous active duty
 - Serving 6 months of active duty for training doesn't count
 - Dishonorable discharge also prevents eligibility

- Eligibility has also been extended to those who have served in Reserves or National Guard for at least six years. VA determines eligibility
- VA issues Certificate of Eligibility, which veteran uses to apply for a VA loan
 - Veteran must apply for certificate and submit most recent discharge/separation papers
- Veteran's surviving spouse may be eligible if he/she hasn't remarried and veteran was killed in action or died of service-related injuries
 - May also be eligible if veteran missing in action or is a prisoner of war

VA Guaranty

- Essential characteristic of VA loans is that they are guaranteed by the U.S. Government
- Guaranty amount available is called "veteran's entitlement"

VA Guaranty - Guaranty Amount

- Guaranty amount is established by VA regulations and has been increased over the years
- World War II guaranty was \$4,000
 - Increased on Sept. 1, 1951, to \$7,500
 - Increased on May 7, 1968, to \$12,500
 - Increased on Dec. 31, 1974, to \$17,500
 - Increased on Oct. 1, 1978, to \$25,000
 - Increased on Feb. 1, 1988, to \$36,000
 - Increased on Jan. 1, 1990, to \$46,000
 - Increased on August 25, 1995, to \$50,750
 - Increased on July 14, 2003, to \$60,000

World War II Guaranty Amount - \$4,000	
September 1951	\$7,500
May 1968	\$12,500
December 1974	\$17,500
October 1978	\$25,500
October 1980	\$27,500
February 1988	\$36,000
January 1990	\$46,000 maximum
August 1995	\$50,750 maximum
July 2003	\$60,000 maximum
2005	\$89,912 maximum
2006 through July 29, 2008	\$104,250 maximum
July 30, 2008 through December 31, 2008	\$104,250 maximum in most counties; higher maximums in high-cost counties, up to a ceiling of \$182,437
2009	\$104,250 maximum in most counties; higher maximums in high-cost counties, up to a ceiling of \$319,265

- Since 2005, the maximum amount has increased. It is no longer a fixed amount, it is now:
 - 25% of Freddie Mac conforming loan limit for a single-family residence.
 - As of 2008, VA sets higher loan amount for high-cost areas
- Not all borrowers get maximum guaranty amount
- VA sets higher maximum guaranty amounts for high-cost areas

- Freddie Mac's loan limit for 2016 is \$417,000
 - VA guarantee is 25% of \$417,000 or \$104,250
 - High-cost area depends on the county's median house price
 - With a maximum guarantee ceiling of 25% of 175% Freddie Mac's conforming limit for one-unit properties in high-cost areas
 - 25% of \$1,094,625 = \$273,656
 - Uses loan limit for conventional loans in high cost areas
 - This figure for 2016 is \$625,500 x 1.75% = \$1,094,625
- Examples of a VA Guaranty based on loan amount
 1. \$75,000 Loan amount between \$56,261 and \$144,000
 × 40% Guaranty: 40% of loan amount, up to \$36,000

 \$30,000 Guaranty amount in any county

Loan Amount	Guaranty Amount
Up to \$45,000	50% of loan amount
\$45,001 - \$56,250	\$22,500
\$56,251 - \$144,000	40% of loan amount, up to a maximum of \$36,000
\$144,001 - \$417,000	25% of loan amount
Over \$417,000	25% of loan amount, up to county maximum

- 2 \$125,000 Loan amount between \$56,261 and \$144,000
 × 40% Guaranty: 40% of loan amount, up to \$36,000

 \$ 50,000 40% of loan amount (exceeds \$36,000)
 \$ 36,000 Guaranty amount in any county
3. \$300,000 Loan amount between \$144,000 and \$417,000
 × 25% Guaranty: 25% of loan amount, up to county maximum

 \$75,000 Guaranty amount in any county
4. \$450,000 Loan amount over \$417,000
 × 25% Guaranty: 25% of loan amount, up to county maximum

 \$112,500 25% of loan amount (exceeds \$104,250)

	\$104,250	Guaranty amount in most counties
	\$110,750	Guaranty in a county where the maximum is \$110,750
	\$112,500	Guaranty in a county where the maximum is \$123,000
5.	\$1,300,000	Loan amount over 417,000
	× 25%	Guaranty: 25 % of loan amount, up to county maximum
	<hr/>	
	\$ 325,000	25% of loan amount (exceeds \$319,265 ceiling)
	\$ 104,250	Guaranty amount in most counties
	\$ 180,500	Guaranty in a county where the maximum is \$180,500
	\$ 319,265	Guaranty in a county where the maximum is at the ceiling

- Up to \$45,000 loan - guaranty 50% of loan amount
- \$45,001–\$56,250 loan - guaranty \$22,500
- \$56,251–\$144,000 loan - guaranty 40% of loan amount, up to \$36,000
- Over \$144,000 - 25% of loan amount, up to maximum of 25% of Freddie Mac limit for single-family residences
- Veteran's guaranty entitlement doesn't expire
 - Available until used by veteran or surviving spouse
- If the borrower sells property and repays loan, the entitlement is restored. A one-time restoration of entitlement will be allowed to the veteran who pays off their loan without selling the property.

Veteran's Liability

The VA guaranty doesn't relieve borrower of personal liability for loan; a lender can foreclose on property in the event of default.

- Borrower may be required to repay VA amount that VA paid lender for default
 - If loan closed on/after January 1, 1990, repayment is only required if veteran was guilty of fraud, misrepresentation, or bad faith
- When VA requires veteran to repay amount VA paid the lender, the debt is considered a delinquent federal debt
 - Vet's federal income tax refunds can be applied to it
 - Any federal pay can be garnished
 - The veteran isn't eligible for any federal loans until arrangements to repay are made
- If lender's foreclosure loss isn't covered by guaranty amount, veteran may be liable to lender for uncovered amount

Assumptions

- VA loans can be assumed by any creditworthy individual
 - Loan closed prior to March 1, 1988 may be assumed without lender or VA approval
 - If closed after March 1, 1988, borrower must obtain a release of liability from VA
 - Otherwise original borrower remains liable
- VA will release original borrower if following conditions are met:
 - Loan must be current
 - Purchaser must be an acceptable credit risk
 - Purchaser assumes veteran's obligations and liabilities on loan in written agreement
 - Veteran requests release of liability from VA

Substitution of Entitlement

A veteran's entitlement is not automatically restored after assumption. It is only restored under certain conditions:

- Assumptor is eligible veteran with entitlement \geq loan's guaranty amount
- Assumptor agrees to substitute entitlement for original borrower's
- Loan payments must be current
- Assumptor must be creditworthy

VA Guaranty - Remaining Entitlement

Full entitlement cannot be restored if the VA loan is assumed by a non-veteran

- Veteran may still have remaining entitlement for another loan
- Remaining is entitlement determined by subtracting amount of entitlement used on original loan from amount of entitlement currently available
 - Currently available entitlement – Guaranty on existing loan = Remaining entitlement
- Generally used when veteran has sold property for which original loan was obtained, since VA loans require owner occupancy
- VA Remaining Entitlement - Example:

Andrea Jordan obtained a VA loan in 1987 and used the maximum guaranty then available, \$27,500. Jordan sold her old home and allowed the non-veteran buyer to assume her VA loan. Now she wants another VA loan to buy a new home in a county where the maximum guaranty is \$104,250. If Jordan wants to borrow \$144,000 or less, her remaining entitlement is \$8,500.

\$ 36,000	Basis for calculation of remaining entitlement
- 27,500	Guaranty on existing loan
<hr/>	
\$ 8,500	Remaining entitlement to be used for new loan

If Jordan wants to borrow \$144,000 or less, her remaining entitlement is \$76,750.

\$104,250	Basis for calculation of remaining entitlement
- 27,500	Guaranty on existing loan
<hr/>	
\$ 76,750	Remaining entitlement to be used for new loan

Entitlement and Co-Ownership

Even if the buyers are both eligible veterans, the maximum guaranty is not increased. If veteran buys home with non-veteran other than spouse, guaranty only covers veteran's half of the loan.

Refinancing with a VA Loan

The Interest Rate Reduction Refinancing Loan/IRRRL can be used to:

- Shorten term
- Reduce monthly principal and interest payment
- Highlights of IRRRL
 - Requires minimum documentation
 - VA does not require a credit check or appraisal
 - Although lender can still require these two items

- 0.5% funding fee
- Can refinance for up to 100% of home's value
- Cannot be used to pay off a second mortgage

The VA offers a cash-out refinance for veterans who have an existing VA home loan and have equity in the property.

- Can be used to pay off a first and second mortgage
- May be able to get cash back
- Can refinance up to 100% of the home's value
 - Dependent upon lender's guidelines
- Funding fee required:
 - 2.15% for first time users
 - 3.30% for subsequent users

The VA also offers a program for veterans to refinance a conventional loan into a VA loan.

- Considered to be a cash-out refinance
- Funding fee of 2.15% for active-duty members
 - Fee can be added to the loan amount
- Can refinance up to 100% of the home's value
 - Dependent upon lender's guidelines

VA Loan Amounts

- VA doesn't set maximum loan amount.
 - Instead, VA loan may not exceed appraised value of property
- VA-approved appraiser appraises property and VA issues a Notice of Value (NOV)
- Most lenders require guaranty to equal 25% of loan amount
 - No-down payment loan over \$417,000 unlikely
- VA Loan Amount w/ Zero Down Payment Example
- A VA loan may not exceed the appraised value of the property. The appraisal must be performed by a VA-approved appraiser and the VA issues a Notice of Value or NOV.

\$104,250	Maximum guaranty amount in most counties
÷ 25%	Percentage of loan amount
<hr/>	
\$417,000	Maximum loan amount with no down payment

VA Loan Amounts - Making a Down Payment

- If veteran wants VA loan larger than \$417,000, she can make down payment
 - Guaranty + down payment = 25% of sales price
- VA Loan Amount Making Down Payment Example

- Robert Mendez wants to buy a home that has been valued at \$450,000. He has full entitlement, and the maximum guaranty for his area is \$104,250. His lender won't make a loan for more the \$417,000 unless Mendez makes a down payment.

\$ 450,000	Sales price
× 25%	Desired ratio of guaranty + down payment to price
<hr/>	
\$ 112,500	25% of loan amount
- 104,250	Maximum guaranty
<hr/>	
\$ 8,250	Down payment required by lender
 \$450,000	 Sales price
- 8,250	Down payment
<hr/>	
\$441,750	Loan amount

VA Loan Amounts - Secondary Financing

- Veteran can finance part or all of down payment if:
 - Combined loans don't exceed NOV
 - Buyer qualifies for combined payments
 - Interest rate on second loan doesn't exceed rate on VA loan

Underwriting Guidelines

- Lenders use standards established by Department of Veterans Affairs to analyze veteran creditworthiness
- Two methods of income analysis for VA loans:
 - Income ratio method
 - Residual income method (cash flow)

Underwriting Guidelines - Income Ratio Analysis

- VA uses total obligations to income ratio to analyze income ratio of potential borrower
- Ratio generally shouldn't exceed 41%
- Installment debts with more than 10 payments left are considered recurring obligations
- VA Income Ratio Analysis Example:

Robin Young is eligible for a VA loan. She and her husband, Mike Appleton, have a combined income of \$6,000 per month. Their monthly obligations, not including their housing expense, add up to \$1,030.

\$ 6,000	Monthly income
× 41%	Maximum debt to income ratio
<hr/>	
\$ 2,460	
- 1,030	Monthly recurring obligations
<hr/>	
\$ 1,430	Maximum housing expense (PITI)

Young and Appleton could qualify for a \$1,430 monthly housing expense under the VA's debt to income ratio rule.

Underwriting Guidelines - Residual Income Analysis

- Residual income analysis (cash flow analysis) is second method used to qualify loan applicant
 - Gross monthly income – Taxes, recurring obligations, housing expenses = Residual income
- Vet's residual income should be at least one dollar more than VA's minimum requirement
- Minimum requirement varies according to:
 - Region of the country
 - Family size
 - Size of proposed loan

VA Residual Income Analysis Example

Example: Continuing with the previous example, suppose Young and Appleton have two children and live in the VA's Midwest region. They're planning to buy a home that costs more than \$80,000. To meet the VA's guidelines, they should have at least \$1,003 in residual income (see below).

\$ 6,000	Gross monthly income
1,100	Federal income tax withheld
250	State income tax withheld
460	Social Security and Medicare withheld
1,030	Recurring obligations
- 1,430	Maximum housing expense (from 41% ratio)
<hr/>	
\$ 1,730	Residual income

Table of Residual Incomes by Region For Loan Amounts of \$79,999 and below				
Family Size	Northeast	Midwest	South	West
1	\$390	\$382	\$382	\$425
2	\$654	\$641	\$641	\$713
3	\$788	\$772	\$772	\$859
4	\$888	\$868	\$868	\$967
5	\$921	\$902	\$902	\$1,004
Over 5: Add \$75 for each additional member up to a family of 7.				

Table of Residual Incomes by Region For Loan Amounts of \$80,000 and above				
Family Size	Northeast	Midwest	South	West
1	\$450	\$441	\$441	\$491
2	\$755	\$738	\$738	\$823
3	\$909	\$889	\$889	\$990
4	\$1,025	\$1,003	\$1,003	\$1,117
5	\$1,062	\$1,039	\$1,039	\$1,158
Over 5: Add \$80 for each additional member up to a family of 7.				

Underwriting Guidelines - Compensating Factors

- VA underwriting standards are merely guidelines, not hard and fast rules
- Compensating factors may allow loan approval in spite of application weaknesses
- Compensating factors include:
 - Excellent long-term credit history
 - Conservative use of consumer credit
 - Minimal consumer debt
 - Long-term employment
 - Significant liquid assets
 - A down payment
 - Little or no increase in housing expense
 - Military benefits
 - Satisfactory previous experience with home ownership
 - High residual income
 - A low total obligations to income ratio
 - Tax credits for child care,
 - Tax benefits of home ownership; and
 - (for refinancing) Significant equity in the property
- Compensating factor must be relevant to weaknesses in application

Underwriting Guidelines - Income Ratio Exceptions

- Special rules for approving applicant whose income ratio is over 41%
- Lender must submit detailed statement to VA, listing compensating factors
- If residual income exceeds minimum by 20% or more, loan can be approved even though vet's income ratio is over 41% without any compensating factors
- VA qualifying rules much more liberal than Fannie Mae/Freddie Mac rules

VA Income Ratio Exceptions Example

Example: Refer back to the previous example involving Young and Appleton. This time assume that they want to buy a house that costs \$218,000. Their monthly housing expense would be \$1,570. With this housing expense added their monthly recurring obligations (\$1,030), their total monthly obligations come to \$2,700. This gives them a 45% debt to income ratio ($\$2,700 \div \$6,000 = 45\%$). Even though the ratio is higher than 41%, the lender may approve the loan if there are compensating factors that justify approval. But no other compensating factors are necessary if the couple's residual income exceeds the minimum by 20% or more. Let's see whether Young and Appleton have enough residual income to bring the 20% rule into play.

\$ 6,000	Gross monthly income
1,100	Federal income tax withheld
250	State income tax withheld
460	Social Security and Medicare withheld
1,030	Recurring obligations
- 1,570	Maximum housing expense (from 45% ratio)
<hr/>	
\$1,590	Residual income

When the \$1,570 housing expense is subtracted from their gross income along with their taxes and other obligations, it leaves Young and Appleton with \$1,590 in residual income. However, the VA requires only \$1,003 in residual income for a family of four in the Midwest region. Now let's see if the couple's residual income exceeds the minimum by 20% or more.

\$1,590	Residual income (with \$1,570 housing expense)
- 1,003	Required minimum residual income
<hr/>	
\$ 587	Residual income in excess of required minimum
\$1,003	Required minimum residual income
× 20%	
<hr/>	
\$ 201	20% of required minimum

Now we will look at the entire qualifying process for a VA loan following the format below:

VA QUALIFICATION FORM

A. Borrower's Income \$ VA Disability 133
 Other Income \$ 4638
 Co-Borrower's Income \$
 Other Income \$
 Rental Income @40% maint \$

TOTAL INCOME: \$ 4771

Less 1205

B. Less Federal Tax \$ 677
 Less State Tax \$ 174
 Less Social Security \$ 354

1205

NET INCOME OF B & CB \$ 3566 Net Income

C. HOUSING EXPENSE:

Loan Amount: 188,550+

Funding Fee (2.15%): 4055

Loan Amount= 192,705

Principal and Interest \$ 865
 Hazard Insurance \$ 243
 Flood Insurance \$
 Property Tax \$ 124
 All monthly revolving debts \$ 0
 All installment debt >6 mos \$ 150

=1232

PTI & ALL MONTHLY DEBTS \$ 1382

D. Maintenance (\$30-\$90) \$ 1700 sq. foot @ .14
 Utilities (\$100-\$250) \$ =238

TOTAL DEBT: \$ 1620

Balance Available for Family \$ 3566-1620= 1946

Support (B minus D)

VA Ratio (<or=41%) 28.9%

C divided by A

TOTAL AMOUNT REQUIRED BY VAN FOR FAMILY SUPPORT:

Loan Amount below \$79,999K
 Family Members/Req. Reserve

Loan Amount \$80K and above
 Family Members/Req. Reserve

- | | |
|----------|-----------|
| 1. \$382 | 1. \$441 |
| 2. \$641 | 2. \$738 |
| 3. \$772 | 3. \$889 |
| 4. \$868 | 4. \$1003 |
| 5. \$902 | 5. \$1039 |

Over 5 add 80 for each additional member up to family of 7

GOOD FAITH LENDING I

Upon completion of this lesson, you should be able to:

- Understand ethics in business and in mortgage lending
- Recognize different types of fraud
- Explain Fraud for Housing
- Detect fraud on the different loan and application documents
- Establish quality control strategies

INTRODUCTION – ETHICS

The mortgage lending industry has set in place many laws regarding ethics. They all result in the same outcome, and that is doing what is best and right for the consumer. This lesson will allow you to see how these laws should be applied. It will also demonstrate how these laws help improve efficiency while ensuring honesty and integrity are upheld by lenders and all those in the lending industry, regarding consumers who are looking to purchase or refinance a home.

First we will talk about ethics and how it can sometimes be confusing with its diversity. The basis of this course is to demonstrate that when it comes to ethics, it's not always black and white. You should always place yourself in a similar situation as the borrower and perform in a manner in which you want others to do unto you, this will help you make the best ethical choice.

Albert Schweitzer felt that ethics was our concern for good behavior and it was not only our consideration for our own personal well-being, but that of others. In a sense, we are considering the concept of the golden rule of do unto others, as you would have them do unto you. Keep this concept in mind as you go through this course. And always ask yourself in any situation, "How would I feel had that action been done to me". Would it have been acceptable to you? If not, then it was probably not ethical.

This is the area where we have the most interesting arguments in the study of ethics. Many professionals assume that if it is legal, then by default it is ethical. There are many laws that, if applied, will impact on our understanding of ethics. It is frightening the number of times I have heard a person say, "Never mind that ethics stuff, is this legal?" Just because it is legal, does not mean it is how one should behave. It is possible for a legal act to be unethical and likewise an ethical act can be illegal. Segregation in this country was for a long time legal. However, it could not be considered ethical. At that time, violating segregation laws would be considered illegal, but ethical.

And so with that in mind, let's begin this lesson on ethics.

BUSINESS ETHICS

Most organizations or businesses establish moral guidelines or a code of ethics to ensure their employees conduct themselves in a proper manner. This will guarantee every consumer is treated with fairness and professionalism. A well-rounded mortgage loan originator takes considerable pride in their diverse knowledge of the industry. Self-discipline is essential; there are company guidelines to abide by and federal acts that were established to ensure all consumers are treated in a consistent non-discriminating manner.

Mortgage lending personnel should be available to assist and educate all consumers in the home loan process. One important job of the mortgage loan originator is to coach the consumer in all steps for pursuing their homeownership dreams, whether it is a first-time homebuyer or someone experienced in loan practices.

Each individual applying for a home loan or someone who is merely shopping for programs, should be treated the same as every person who comes through the door.

Lenders may not reveal information about the buyer's loan without permission from the borrower. Please keep this in mind. While others in the real estate industry may want to know what is going on, you are not entitled to give any of this information to other sources, such as the appraiser or realtor unless the consumer wants to reveal it. Do not be pressured by those who refer business to you to disclose information that is confidential. Always maintain your ethical standards. Professionals in the mortgage lending industry should not assume that the relationship they have with you will depend on you violating confidentiality to keep you happy. For instance, if a realtor wants information on the borrower, they need to ask the borrower for the information. There are some real estate professionals who often feel entitled to confidential information from mortgage lenders.

As an example, here are two different relationships in the financed transaction. There is the relationship of the real estate agent with the client and another entirely separate relationship between the buyer and the lender. Information should only travel between the two relationships. That is between the lender and the borrower and between the real estate agent and the borrower. Confidential information on the borrower should never travel between the lender and the real estate agent.

FRAUD

As in any industry there are those individuals who choose not to follow guidelines set forth by their company or the laws of their industry. Those persons need to be aware if they choose to commit fraud in the lending industry there are fines, and depending on the severity of the fraud or ethics crime, jail time. In some jurisdictions fraud is considered a felony and could include:

- Fines and/or make financial restitution
- Suspension or loss of professional license

Real estate professionals should be familiar with the laws governing fair housing. Discrimination in housing based on race, religion, gender, color, national origin, handicap, or familial status is prohibited. The penalties for violation can be severe. This is not to say that some people might suggest, often subtly, that the laws be overlooked. In some cases, the public is not aware of the specifics of the laws and must rely on their mortgage lender to advise them. Regardless if you feel the laws are just or applicable, the fact remains that these laws must be followed. Do not get involved in trying to circumvent the law and risk losing your career opportunity.

The Home Mortgage Disclosure Act (HMDA), Real Estate Settlement Procedures Act (RESPA), Home Ownership and Equity Protection Act (HOEPA), Equal Credit Opportunity Act (ECOA), Truth in Lending Act (TILA), Gramm-Leach-Bliley Act, are some of the laws that have procedures in place for mortgage lenders to follow regarding ethics in lending. We will discuss some of these laws in the next section of ethics.

QUALITY CONTROL

Fraud prevention and detection programs are in place to investigate and prosecute individuals involved in fraudulent schemes. Freddie Mac recommends those in the mortgage lending industry be aware of these deceptive plots. They recommend lending companies provide quality control tactics and train personnel to detect and prevent fraud. Quality control programs could include regular updates on compliance information, a document checklist, fraud detection practices, and red flag situations.

Freddie Mac has established practices for fraud prevention on their website including employee training and fraud awareness in loan origination and servicing areas. Also provided on this website is a list of investigative resources to assist mortgage lenders in exploring the possibility of fraud and/or suspected misrepresentation.

Warehouse lenders should implement a strong screening process and fund only legitimate loans. They should also have a mechanism in place to manage funds from investors.

All those involved in the loan process from beginning to end should practice ethical behavior; this should be always first and foremost with every application. Consistency in honesty regarding the buyers and sellers in a transaction should always come naturally. Never practice "money under the table" and make sure all items are documented and accurate on application and closing documents. The closing agent should review documents for the loan with the borrower and check that all charges are legitimate. Employers should provide honest information regarding wages and expenses and the self-employed borrower should provide accurate supporting documents. The consumer should give true and accurate information on their application along with reliable paperwork needed to complete the loan process.

DIFFERENT TYPES OF FRAUD

Fraud is deception against another person. Shams could come in the form of an act, an expression, an omission, a concealment or a misrepresentation. All these are considered a felony.

The FBI lists two categories of mortgage fraud - fraud for profit and fraud for housing. Fraud for profit is usually committed by those in the lending industry while fraud for housing is typically perpetrated by the borrower.

An example of those who commit fraud for profit could be an appraiser who is persuaded to give a fraudulent market value. This plot may include the mortgage loan originator and/or one or more realtors.

Fraud for Profit involves criminals with the intent to deceive. These individuals do not intend to pay back the loan. The objective in fraud for profit could be one or more of the following:

- To inflate the value of property
- Provide false income and credit info
- Remove the equity
- Abandon the home and payments

Involved in the scheme are individuals in the mortgage lending industry who may commit multiple transactions with misrepresentations and omissions. Those in the industry involved in the plot could be the loan originator, appraiser, real estate agent, processor, or the underwriter. There are situations when the buyer and seller are involved and times when the borrower is unaware of the conspiracy.

Fraud for Housing - This occurs when the borrower is the perpetrator and acquires a home under false pretenses by falsifying supporting loan documents. There are four categories of Fraud for Housing:

- Occupancy
- Cash to close
- Income to qualify
- Appraisal

Occupancy fraud is when a borrower attempts to borrow money for an investment property but states on the loan application that this will be their primary residence or a second home. By doing this the borrower will usually receive more favorable loan terms, such as a better interest rate and less money needed for the down payment. The borrower also benefits by avoiding the payment of capital gains taxes on the investment.

Asset or Down Payment Fraud - Funds for down payment, closing costs, etc., can be verified using a couple of different methods; the Verification of Deposit and the most recent two months of bank statements. The lender always handles the delivery of the Verification of Deposit (VOD). Once the VOD is completed, an examination of this document should include looking for a large increase or new account; if either of these is the case, the borrower must explain the reason(s) in writing. Also, compare ending balance figures from the previous month's bank statements to see if it matches the current bank statement. On the VOD form be aware of rounded dollar amounts, significant changes in balances in short periods of time, borrower's name is not listed on the account, information is crossed out, white-out has been used, and/or fees have been collected for insufficient funds.

Income Fraud - There are two key factors regarding a borrower's employment, their employment stability and quantity of income. To establish income, the borrower will need two years of employment verified with any gaps explained in writing.

The Verification of Employment should be mailed to the employer or hand-delivered by the lender to the employer. Mortgage loan originators should check for deletions, cross outs or numbers that appear to be squeezed in on a handwritten verification of employment. Always perform an internet search of the employer's business name, and phone number to guarantee it does not reference back to a third party involved in the mortgage loan transaction.

A few other areas to look for fraud on the VOE would be:

- Check to see if the employer's address is a post office box only
- Employer's phone number is a cell phone but there is an established office
 - Borrower's office number phone number and home number are the same but the applicant did not specify self-employed on the loan application
- Applicant's income level is not consistent with the profession listed on the application

The check stubs submitted by the borrower should be examined to make certain the company name and/or employer name is not handwritten. Also, income should be listed in exact figures. The social security number should match information provided on the loan application documents.

If the borrower is related to the employer further investigation is required, such as an investigation of the borrower's W-2. This form should be labeled the "borrower/employee copy" and have a consistent font throughout.

Self-employed borrowers should provide tax returns that are signed and dated. Also check to see if the address or profession is consistent with information on the loan application, the handwriting or font throughout return is the same, and there is no evidence of whiteouts.

Appraisal Fraud - There are times when pressure is placed on the appraiser, by other professionals in the lending industry, to inflate a home's value. This type of activity is considered fraudulent. Individuals may convince the appraiser to embellish a value, for example to collect a portion of the illegal profits. Any type of activity involving the misrepresentation of an appraisal is considered fraud. This type of fraud not only impacts the buyer, but the lending industry as a whole. If improper values are misrepresented by fraudulent means, this will have an adverse affect on the use of this sale as a dependable comparable.

Mortgage lending personnel should review the appraisal's content to look for fraud. Some signs would be: subject property has increased in value, but other homes in same area are declining. Perhaps the comparables do not match the subject or there is no data source for the comps to show recording information. Other signs would be the photo of the subject property will have a "for sale" or "for rent" sign in the front yard when this is a refinance transaction.

The Appraisal Foundation is authorized by Congress as the source for appraisal standards and qualifications. Their mission statement is:

The Appraisal Foundation is dedicated to promoting professionalism and ensuring public trust in the valuation profession. This is accomplished through the promulgation of standards, appraiser qualifications, and guidance regarding valuation methods and techniques.

Appraisal management companies are required to register with, and be subject to, supervision by state appraiser regulatory agencies and verify that only licensed and certified appraisers are used for federally related transactions. These appraisal management companies are also required to comply with the regulations of the Uniform Standards of Professional Appraisal Practices.

OTHER AREAS TO DETECT FRAUD

Credit Report Fraud - The Credit report is another good source for detection of fraud in the mortgage loan transaction. Check to the make certain the social security number and all personal information is consistent with the loan application documents. Some items of concern on the credit report might be the social security number is not valid, the employment start date is inconsistent with information provided on the loan application, and/or all accounts have zero balances. Also make sure the credit history is consistent with the applicant's income, employment, and age.

Sales Contract Fraud - The sales agreement should be checked by lender for validity. There are portions of the agreement that would present red flags, such as:

- Borrower is not the same as purchaser
- Sales price is significantly less than market value
- No realtors are involved
- A second mortgage is shown

Whether the home is listed with a Realtor or is For Sale By Owner (FSBO), a purchase contract or sales agreement is recommended and should be executed by all parties involved. The sales contract makes the transaction a binding agreement. It will list all conditions between buyer and seller and constitutes an acceptance of offer. It is usually accepted with a deposit from buyer otherwise known as an Earnest Money Deposit.

The sales contract should also contain, but are not limited to:

- Options for financing include either
 - A mortgage loan
 - An assumption
 - Seller financing
- Legal information
 - Legal description of the property
- Date the loan must close
- Closing costs paid by each party
- Seller must deliver clear title
 - If defects are present, seller must cure

You will want to review the Closing Disclosure Form for areas of fraud. These sections include, but are not limited to, checking to see if the sales price at closing and the sales price on the sales agreement are the same amounts. Other places might be if the borrower does not owe any money or check if there is an indication of an undisclosed second mortgage.

Loan Application Fraud - The loan application should be thoroughly examined to determine if fraud is present.

- Certain sections to search for fraudulent employment information could be:
 - Are the number of years on their current job consistent with their age?
 - Assets column
 - Substantial assets should equal ample credit
 - Is the home large enough to accommodate all occupants?
 - Do the debts listed match the credit report?
 - Is the property being purchased from a landlord or an employer?
 - Down payment is something besides cash such as
 - Gift funds
 - Personal property
 - Borrower is purchasing a second home but it is within a close distance to his primary home
 - Borrowers work location is not a practical distance from location of home being purchased

TYPES OF FRAUD

Straw Borrower - This imposter acts like the real borrower. They are allowed to use another person's name and credit history while the real borrower is kept secret to gain loan approval. Basically they are making the home purchase on behalf of another person. Sometimes a straw borrower is used in cases where the real borrower may have poor credit or, for any other reason, they are unable to obtain a loan with their own personal information.

Although a straw borrower is not necessarily illegal in all circumstances, it is considered fraud if used in situations where the actual borrower may:

- Not have the income or credit history
- Not intend to occupy the home as a principal residence
- Not a legal alien
- Not be eligible for a special purpose loan
- Intend to use the property for flipping

With this illegal technique, the bank is put in a higher default risk for the loan plus the person acting as the straw borrower can also be held liable for this type of transaction.

Air Loans - air loans are loans with no underlying collateral as security for the loan; nothing but "air" securing the loan. A property and borrower are fictitious, therefore when the loan goes into default the lender loses everything because the house never existed. The person behind this type of scheme will use a system of phone banks and mailboxes for verification of employment, rent or mortgage, credit history, title information, etc. The loan application and closing process are all based on misrepresentations by the fabricated borrower and property.

As in the case of a straw borrower having a phony borrower, air loans are made to a fake borrower on property that does not exist.

Red flags for air loans would be the same as the straw borrower. Others might include:

- There is no real estate agent involved
- Mortgage payments are not made by the borrower
- Chain of title on property cannot be validated

BUILDER BAILOUT - Occurs when a builder has trouble moving property. They may use a relative to secure a fake sale. Or they may offer dishonest bargains like no money down or a silent second. Some red flags on this type of scam would be if the borrower barely qualifies or their source of funds is questionable. Another red flag would be if the lender has knowledge of the builder and borrower being affiliated with each other. This would need to be checked out to ensure and document the transaction is not deceptive.

Flips - Property flipping is a legal transaction when ownership of a property will change several times over a short period of time.

Illegal flips or flipping is when a home is purchased at an inflated appraised value. The purpose here is to obtain a larger loan and skim the equity off of the property. This will mislead a buyer into thinking the home is worth more. The seller and appraiser (and sometimes others in the lending industry) convince the appraiser to inflate the value of the home. The unknowing borrower starts out with negative equity.

Another illegal flip is when renovations are falsely documented as having been made within the appraisal report. When in fact, only minor cosmetic improvements were made. Again the borrower buying the home is unaware of the inflated value and may be getting into a negative loan position.

Red flags needing further investigation to determine if this is an illegal flip would include:

- Multiple changes of ownership in a short period of time
 - Appraised value increases each time
- Seller of the property is not listed on the property's title
- An association exists between parties to the transaction
- Seller has owned property for a very short time period

Affinity Fraud occurs when one or more members of a group, for example religious, military, or perhaps a professional group, are involved in perhaps an investment property scheme or fraudulent foreclosure rescues. These groups thrive because they develop a level of trust within the membership and members may be embarrassed because of profits earned at the cost of other individuals (although these members were unaware at the time of the scheme). These "pretend members" figure those who are honest affiliates of this group will not want their organization to develop a bad reputation, so instead they choose to remain silent.

Identity Theft - occurs when a person steals personal information from another individual to use for their own financial gain. Identity theft, sometimes referred to as identity fraud, is considered a crime. Individuals steal another person's personal information for their own financial gain, and in some cases, taken over another individual's identity all together. Trying to retrieve and restore a credit reputation once it is stolen is a lengthy and tedious process.

Some types of identity theft that can occur on a mortgage loan application include an underhanded spouse who wants to refinance and pay off debt or finance a secret second life.

Identity thieves can steal another person's:

- Social security number
- Bank account numbers
- Credit card numbers
- Phone card security code information

It is easy for criminals to obtain personal information to commit identity theft. Some common ways are:

- Dumpster diving
 - Going through a person's garbage cans and finding:
 - Copies of checks, credit cards, bank statements, etc.
 - Discarded preapproved credit cards received in the mail
- Shoulder surfing
 - Watching as someone enters the security code on their debit card during a transaction in a department or grocery store
 - Listening in on a phone conversation as the person gives their credit card information to perhaps book a vacation or hotel stay
- Internet
 - Responding to spam that request identification

The Department of Justice passed the Identity Theft and Assumption Deterrence Act in 1998 which prohibits the use of another person's identity to commit fraud or any unlawful act that violates Federal Law or any applicable State or local law. Most offenses carry a maximum term of 15 years' imprisonment, a fine, and the forfeit of any personal property used or intended to be used in committing the offense.

GOOD FAITH LENDING II

Upon completion of this lesson you should be able to:

- Familiarize yourself with the history of the Fair Housing Act
- Understand the rules associated with the Equal Credit Opportunity Act
- Recognize the provisions related to the S.A.F.E. Lending Act, the Mortgage Assistance Relief Services Act (MARS), the Gramm-Leach-Bliley Act (GLBA), and the Bank Secrecy Act/Anti- Money Laundering Act (BSA/AML)

Fair Housing Act - Fair housing laws date back to the 1960's when a political movement was set in force to prohibit discrimination in housing. On April 11, 1968, one week after the assassination of Martin Luther King, Jr., Pres. Lyndon Baines Johnson signed the Civil Rights Act of 1968, Title VIII; this act is also known as the Fair Housing Act of 1968.

The Fair Housing Act was implemented to prevent discrimination in housing by protecting buyers and renters. The objective of this act was to create a unitary housing market where a person's race/color, national origin, religion, sex, disability, or familial status would not prevent them from purchasing or renting a home. Initially, the Fair Housing Act prevented discrimination based on race, color, religion, sex and national origin. Disability and familial status were added in 1988.

The Department of Housing and Urban Development (HUD) conducts surveys to insure minority buyers receive fair treatment and the same treatment as others during the mortgage lending process.

The rules under FHA include pre-application customers; those potential borrowers wanting only information about a home loan. This law protects the potential applicant too; they should be encouraged to inquire about homeownership and counseled on how to proceed with their dream of owning a home. Also included is discrimination in appraising property, refusal to purchase a loan, or setting different terms or conditions for purchasing a loan. Basically any type of discrimination in the mortgage lending industry will not be tolerated.

The Office of Fair Housing and Equal Opportunity (FHEO) administers and enforces federal laws. They also establish policies so all people have equal access to the housing of their choice. Particular activities carried out by the Office of Fair Housing and Equal Opportunity consist of implementing and enforcing the Fair Housing Act and other civil rights laws, including:

- Title VI of the Civil Rights Act of 1964
- Section 109 of the Housing and Community Development Act of 1974
- Section 504 of the Rehabilitation Act of 1973
- Title II of the Americans with Disabilities Act of 1990
- The Age Discrimination Act of 1975
- Title IX of the Education Amendments Act of 1972
- The Architectural Barriers Act of 1968.

Redlining is the practice of denying, or increasing the cost of services, to residents in certain neighborhoods, based on race or ethnic background. The term "redlining" was coined in the late 1960s, and it describes the practice of marking a red line on a map to define the area where banks would not invest. Later the term was applied to discrimination against a particular group of people by race or sex. At first areas most frequently discriminated against were black inner-city neighborhoods.

The Fair Housing Act prohibits the practice of redlining when the criteria is based on race, religion, gender, familial status, disability, or ethnic origin. Although a lender may legally refuse to make a loan because of property values in a declining neighborhood.

Equal Credit Opportunity Act (ECOA) – Regulation B

In the following sections, "CFR" stands for "Code of Federal Regulations" and "USC" stands for "United States Code". Once Congress passes a law it is recorded in the United States Code (USC) books, but it usually will not explain what procedures should be followed. The Code of Federal Regulations (CFR) explains how the laws are to be implemented.

The Equal Credit Opportunity Act (ECOA), Regulation B, was passed in 1974 and applies to all consumer credit. The definition of consumer credit under the ECOA is:

Credit extended to an individual for personal, family, or household purposes [Regulation B 12 CFR §1002.2(h)]

The purpose of the Equal Credit Opportunity Act is: [Regulation B 12 CFR §1002.1(b)]

- *(b) Purpose.* "The purpose of this regulation is to promote the availability of credit to all creditworthy applicants without regard to race, color, religion, national origin, sex, marital status, or age (provided the applicant has the capacity to contract); to the fact that all or part of the applicant's income derives from a public assistance program; or to the fact that the applicant has in good faith exercised any right under the Consumer Credit Protection Act.
- The regulation prohibits creditor practices that discriminate on the basis of any of these factors. The regulation also requires creditors to notify applicants of action taken on their applications; to report credit history in the names of both spouses on an account; to retain records of credit applications; to collect information about the applicant's race and other personal characteristics in applications for certain dwelling- related loans; and to provide applicants with copies of appraisal reports used in connection with credit transactions."

The ECOA, Reg-B, prohibits discrimination based on: [Regulation B 12 CFR §1002.1(b)]

- Race/color
- Religion
- National origin
- Sex
- Marital status
- Age
- Public assistance

It is illegal to base lending decisions on assumptions of creditworthiness. Although the lender may ask about applicant's age or marital status [Regulation B 12 CFR §1002.13 (a)(iii)(iv)], they cannot ask about the applicant's childbearing plans [Regulation B 12 CFR §1002.5 (d)(3)]

The chart below shows how the Fair Housing Act and the Equal Credit Opportunity Act prohibit the same type discrimination:

FHA	ECOA
RACE	RACE
COLOR	COLOR
RELIGION	RELIGION
NATIONAL ORIGIN	NATIONAL ORIGIN
SEX	SEX

This chart demonstrates the differences in these two acts:

FHA	ECOA
HANDICAP	MARITAL STATUS
FAMILIAL STATUS	AGE
	ALL OR PART OF APPLICANT'S INCOME COMES FROM PUBLIC ASSISTANCE

The Equal Credit Opportunity Act was established to grant all consumers an equal chance to obtain credit. This law requires lending institutions and mortgage brokers to perform specific actions. Included in this law is anyone involved in granting credit: [Regulation B 12 CFR §1002.1]

- Real Estate Brokers who arrange financing
- Small loan and finance companies
- Retail and department stores
- Credit card companies
- Credit unions

Lenders must comply with ECOA in regards to any credit transaction: [Regulation B 12 CFR §1002.1(a)(b)(c)(d)(1)(2)(e)]

- Interviewing/communicating with applicants
- Analyzing applicants' finances
- Offering credit terms to applicants

The Equal Credit Opportunity Law was put in place to:

- Protect individuals and businesses applying for credit
- Establish equality to the many consumers who apply for credit to:
- Finance the purchase or remodeling of a home
- Acquire a small business loan or to help fund an education

The ECOA enforces fair credit lending practices in the taking of loan applications. Here are some guidelines to follow:

- During the loan application process, the mortgage loan originator should ensure the client's best interests are always first and foremost
- The mortgage loan originator may not make any oral or written statement that would discourage an applicant or potential applicant, from making or pursuing a loan application [Regulation B 12 CFR §1002.4(b)]

This rule applies to:

- The application process
- Advertising
- Any method of promoting loan services

The mortgage lending industry should:

- Promote homeownership to all people
- Encourage and counsel potential and existing clients

The federal government requires lenders to report information regarding the applicant when applying for credit primarily for the purpose of [Regulation B 12 CFR §1002.13(a)]

- Obtaining a dwelling
- Refinancing a dwelling
- Occupied (or to be occupied) by the applicant

The required information to be reported is as follows [Regulation B 12 CFR §1002.1 (a)(i)(ii)(iii)(iv)]:

- Race or national origin
- Sex
- Marital Status
- Age

The categories used for race or national origin will be [Regulation B 12 CFR §1002.1(a)(i)]:

- American Indian or Alaska Native
- Asian
- Black or African American
- Native Hawaiian or other Pacific Islander
- White

The categories for ethnicity will be either [Regulation B 12 CFR §1002.1(a)(i)]:

- Hispanic or Latino
- Not Hispanic or Latino

“The applicant(s) shall be asked but not required to supply the requested information. If the applicant(s) chooses not to supply the information or any part of it, that fact shall be noted on the form. The creditor shall then also note on the form, to the extent possible, the ethnicity race, and sex of the applicant(s) on the basis of visual observation or surname”
[Regulation B 12 CFR §1002.13(b)]

The Marital Status category will allow the use of [Regulation B 12 CFR §1002.1(a)(iii)]:

- Married,
- Unmarried (includes single, divorced, and widowed persons)
- Separated

Spouse or Former Spouse Info

The following information will pertain to a spouse or former spouse. It will also provide information regarding what the lender is allowed to request:

- If the client lives in a community property state or is relying on property located in such a state, the lender is permitted to request information concerning an applicant's spouse [Regulation B 12 CFR §1002.5 (c)(2)(iv)]
- Information regarding a former spouse may be requested if the applicant is relying on alimony, child support, or separate maintenance as a means for repayment of the debt [Regulation B 12 CFR §1002.55 (c)(2)(v)]
- If a client is applying for a separate unsecured debt the mortgage loan originator is not allowed under the Equal Credit Opportunity Act to request marital status, unless the applicant lives in a community property state [Regulation B 12 CFR §1002.5 (c)(3)(d)(1)]
- The states with community property laws are:
 - Arizona
 - California
 - Idaho
 - Louisiana
 - Nevada
 - New Mexico
 - Texas
 - Washington
 - Wisconsin

To clarify the rules regarding spousal information, a creditor may request information on a spouse when:

- The spouse will be permitted to use the account [Regulation B 12 CFR §1002.5 (c)(2)(i)]
- The spouse will be liable on the account [Regulation B 12 CFR §1002.5 (c)(2)(ii)]
- The applicant is relying on the spouse's income as a basis for repayment of the debt [Regulation B 12 CFR §1002.5 (c)(2)(iii)]
- The applicant resides in a community property state or is relying on property located in such a state as a basis for repayment of the debt [Regulation B 12 CFR §1002.5 (c)(2)(iv)]
- The applicant is relying on alimony, child support, or separate maintenance payments from a spouse or former spouse as a basis for repayment of the credit requested [Regulation B 12 CFR §1002.5(c)(2)(v)]

Age Discrimination

Age may not be a consideration in the loan decision process provided that the applicant has the capacity to enter into a binding contract [Regulation B 12 CFR §1002.6 (b)(2)(i)]

Certain situations to consider where age may be a factor are:

- Applicant is too young to sign the application (or any legal contract) [Regulation B 12 CFR §1002.6 (b)(2)(i)]
- In most states the legal age is 18 years old
- Client is 62 years old or older [Regulation B 12 CFR §1002.2 (o)]
- Consideration may be given to grant credit in favor of the applicant [Regulation B 12 CFR §1002.6 (b)(2)(iv)]
- When age is a positive factor it can be used to extend credit

Other factors allowing age to be a consideration

- Client is near retirement age [Regulation B 12 CFR §1002.6 (b)(5)]
- Creditor can consider the client's occupation and length of time until retirement
- Income may decrease and this could possibly have a negative impact on the client's ability to re-pay the credit obligation
- Evaluate applicant's retirement income to see if it will support the loan through to maturity
- Evaluation should be made on a case by case basis
- Always assess the borrower's other elements of creditworthiness

The mortgage loan originator is allowed to ask the client for information regarding outstanding debts [Regulation B 12 CFR §1002.6 (b)(6)(i)]

Other information allowed to be collected is [Regulation B 12 CFR §1002.5 (c)(3)]

Name and address under which the accounts are listed

Former names used by the client to obtain credit in the past

Childbearing, Childrearing

In regards to childbearing and childrearing the ECOA allows a mortgage loan originator to inquire about the [Regulation B 12 CFR §1002.5 (d)(4)]

- Number of dependents the applicant has
- The dependent's ages
- Dependent-related financial obligations or expenses, provided such information is requested without regard to:
 - Sex,
 - Marital status
 - Any other prohibited basis

The following inquiries will not be allowed:

- The loan originator may not inquire about the consumer's
 - Childbearing
 - Childrearing
 - Birth control practices
 - Whether they are able to bear children

Required Disclosures

The mortgage loan originator shall provide an ECOA disclosure notice to each client [Regulation B 12 CFR §1002.9 (3)(ii)(b) (all)]

- Sometimes referred to as an ECOA Disclosure
- Explains the purpose of the Equal Credit Opportunity Act and the consumer's rights pertaining to this Act
- Recognizes the Federal Agency that administers compliance with the Equal Credit Opportunity Law
- Supplies their address to consumer should they decide to submit a complaint

The Equal Credit Opportunity Disclosure will:

- Advise the consumer of their rights
- Discuss the applicant's right to disclose or not to disclose income from alimony, child support or separate maintenance

The consumer has the right to know whether their credit application was accepted or rejected within 30 days of filing a completed loan application [Regulation B 12 CFR §1002.9 (a)(i)] An application is considered complete once a creditor has obtained all the information it normally considers in making a credit decision [Regulation B 12 CFR §1002.2 (f)]

- Application means the submission of a borrower's financial information, oral or written, using procedures in line for the type of credit requested.
- Completed Loan Application means the creditor has received all information usually obtained to make a credit decision for the amount and type of credit requested. Information will include, but will not be limited to:
 - Credit report
 - Additional information requested
 - Approvals or reports by governmental agencies needed to guarantee, insure, or provide security for the loan[Regulation B 12 CFR §1002.2 (f)]

The rules of the ECOA require the consumer to receive either of the following within 30 days of filing a completed loan application [Regulation B 12 CFR §1002.9 (a)(i)]

- Approval
- Adverse Action
- Counteroffer

The notification for approval can be:

- Expressed
- Implied

An incomplete application would be a denial for incompleteness and also the following: [Regulation B 12 CFR §1002.9 (c)(1)(i) and (ii)]

- Applicant could complete the application but chose not to
- Creditor lacked sufficient data to warrant a credit decision

If an application is incomplete but there is enough information to grant a denial, the following apply: [Regulation B 12 CFR §1002.9 (c)(1)(i)]

- Applicant must be given the specific reason for the denial
- Notice of right to receive the reasons
 - Incompleteness of the application cannot be given as the reason for denial

Notice of Adverse Action Form - ECOA Notice

If the application for credit is rejected, the lender must disclose specific reasons to the client for rejection [Regulation B 12 CFR §1002.9 (a)(2)(i)]

- The reasons for rejecting the credit file should be clear and concise [Regulation B 12 CFR §1002.9 (a)(2)]
- Indefinite or vague reasons are illegal

It is important to always give explicit details when explaining the reason for denial.

The notification of adverse action is required to be in writing and must contain the following [Regulation B 12 CFR §1002.9 (a)(2)]

- A statement of action taken
- The name and address of the lender
- A statement of the provision known commonly as the ECOA Notice
- The name and address of the federal agency that administers compliance with respect to the lender
- Either a statement of specific reasons for the action taken or a disclosure of the applicant's right to a statement of specific reasons within a specified period of time

If the application was taken by phone, the following apply: [Regulation B 12 CFR §1002.9 (C)]

- Requirements are satisfied when the bank provides an oral statement of :
 - Action taken
 - Applicant's right to a statement of reasons for adverse action

Appraisal Notification

Mortgage lenders are required to notify applicants of their right to receive a copy of the appraisal . Under ECOA the following will apply regarding appraisal notification: [Regulation B 12 CFR §1002.14 (a)(2)(i)]

- The client will receive a "Right to Receive a Copy of Appraisal" including the address, phone number, and contact name of lender [Regulation B 12 CFR §1002.14 (a)(2)(i)]
- A creditor may provide a copy of the appraisal as a
 - Routine delivery [Regulation B 12 CFR §1002.14(a)(1)]
 - Whether credit is granted or denied, or,
 - Upon written request from applicant [Regulation B 12 CFR §1002.14 (a)(2)]
 - A creditor that does not routinely provide appraisal reports shall provide a copy upon an applicant's written request
 - Generally, within 30 days of written request
 - Notice
 - A creditor that provides appraisals only upon request [Regulation B 12 CFR §1002.14 (a)(1)]
 - Must provide applicant with right to receive copy of appraisal notice
 - Can be given at any time, but no later than notice of action taken
 - Delivery - For creditors that provide appraisals only upon request
 - Creditor will deliver/mail appraisal
 - Within 30 days of request [Regulation B 12 CFR §1002.14 (a)(2)(i)(ii)],
 - When report is received, or
 - When reimbursement is received for the report
 - Whichever is the last to occur
 - Deadline for request from applicant is 90 days
 - A creditor need not provide a copy of the appraisal when the request is received 90 days after notice from creditor or 90 days after application is withdrawn

S.A.F.E. Licensing and Registration Rules

The Housing and Economic Recovery Act (HERA) of 2008, addresses the mortgage crisis by including the Secure and Fair Enforcement for Mortgage Licensing Act - S.A.F.E. or SAFE Act. Under the SAFE Act, individual employees of Agency-regulated institutions must register with the Federal Registry.

The Wall Street Reform and Consumer Financial Protection Act (CFPB) of 2010 ("The Dodd-Frank Act") transferred the authority to develop and maintain the Federal Registry from the Agencies to the CFPB. The SAFE Act statute requires individual mortgage loan originators employed by "Agency-regulated" institutions to be registered with the Nationwide Mortgage Licensing System and Registry (Federal Registry), a database established previously by the Conference of State Bank Supervisors (CSBS) and the American Association of Residential Mortgage Regulators (AARMR) to support the licensing of mortgage loan originators by the States.

Under the SAFE Act, a mortgage loan originator is defined as an individual who [SAFE Act 12 USC §5102 A(i-iv)(B),(C),(D),(i-v)(5)(B)(i-ii)]

- Takes a residential loan application, and
- Offers or negotiates terms of a residential mortgage loan for compensation or gain

This definition will not include:

- An individual who performs only administrative or clerical tasks
- Certain individuals who perform real estate brokerage activities
- Individuals who are involved in the extension of credit related solely to time share plans

The SAFE Act is designed to prevent abusive, predatory practices during loan origination and has these provisions for originators:

- Register with the Registry and maintain their registration.
- Obtain a unique identifier through the Registry that will remain with that originator, regardless of employment changes. Mortgage loan originators and their employing institutions must provide MLO unique identifiers to consumers.

Agency-regulated institutions must:

- Require their employees who are mortgage loan originators to comply with these requirements.
- Adopt and follow written policies and procedures to assure compliance with the registration requirements.

The SAFE Act requires all loan originators to be either federally registered or state-licensed [SAFE Act 12 USC §5103 (a)(1)(A)(B)]

- Registered loan originator - employed by depository institution or subsidiary [SAFE Act 12 USC §5102 (7)(A)(i)(ii)(I)(II)(iii)(B)]
- State-licensed loan originator - all others must have state license [SAFE Act 12 USC §5102 (11)(A)(B)(i)(ii)(iii)(B)]
- Loan Processor or Underwriter – supervised loan processors and underwriters who do not perform any activities of a loan originator are exempt from licensing [SAFE Act 12 USC §5103 (b)(1)]
- Registration and licensing are required for independent contractors performing clerical, processor, or underwriter duties [SAFE Act 12 USC §5102 (3)(C)]
 - Independent contractors - may not engage in residential mortgage loan origination activities as a loan processor or underwriter unless they are registered and licensed [SAFE Act 12 USC §5103 (b)(2)]

Real estate agents:

- Generally exempt from S.A.F.E. licensing rules [[SAFE Act 12 USC §5102 (3)(A)(II)(iii)]
 - Must have originator's license if compensated by a lender or mortgage broker for helping to arrange a loan [SAFE Act 12 USC §5102 (3)(A)(II)(iii)]

Other S.A.F.E. Provisions

- Uniform license applications and reporting requirements for states [SAFE Act 12 USC §5101 (I)]
- Improved information tracking across state lines (background checks, fingerprinting, etc.) [SAFE Act 12 USC §5101 (4)]
- Enhanced consumer protection and anti-fraud measures [SAFE Act 12 USC §5101 (6)]
- Fiduciary duties for loan originators [SAFE Act 12 USC §5101 (8)]

Originator's Fiduciary Duties

- Traditionally, mortgage broker:
 - Wasn't buyer's agent
 - Did not have duty to help buyer choose best financing option or to act in buyer's best interests
- Some states have laws giving mortgage brokers fiduciary duties to buyers [SAFE Act 12 USC §5101 (8)]
 - Means mortgage loan originators must act in the best interest of the consumer
 - To the greatest extent possible
- S.A.F.E. now imposes fiduciary duties as a matter of federal law in some states
 - Fiduciary means a legal or ethical relationship of trust between two or more parties

Mortgage Assistance Relief Services Rule - MARS – 12 CFR §1015, Regulation O

The following is a segment from a report on FTC.org dated February 10, 2011 regarding The Mortgage Assistance Relief Services Rule (MARS) and a ban on the collection of up-front fees:

"As of January 31, 2011, companies that offer to help homeowners get their loans modified or sell them other types of mortgage assistance relief services are no longer allowed to charge up-front fees. Under the rule, a mortgage assistance relief company may not collect a fee until the consumer has signed a written agreement with the lender that includes the relief obtained by the company. When the company presents the consumer with that relief, it must inform the consumer, in writing, that the consumer can reject the offer without obligation and, if the consumer accepts, the total fee due. Before the consumer agrees to accept the mortgage relief, the company must also provide a written notice from the lender or servicer showing how the relief will change the terms of the consumer's loan (including any limitations on a trial loan modification)."

In this same report FTC Chairman Jon Leibowitz had this to say:

"Banning the collection of up-front fees will protect homeowners from being victimized. This is especially important at a time when so many people are behind on their mortgages or facing foreclosure."

The Mortgage Assistance Relief Services program (MARS) has the following perimeters:

- FTC rule banning providers of mortgage foreclosure rescue and loan modifications from:
 - Collecting fees until homeowners have a written offer the homeowner decides is acceptable [Regulation 0, 12 CFR 1015.5 (a)]
- Highlights of MARS
 - The following information must be clearly and prominently disclosed upfront: [Regulation 0, 12 CFR 1015.3(a)(b)(1)(2)(3)(i-vi)(2)(d)(1)(2)]
 - The total cost
 - That they can stop using services at any time
 - There is no association with government or lender
 - Homeowner's lender may not agree to change terms of their mortgage
 - Homeowner should not be advised to stop communicating with their lender
 - No advance fees until homeowner has an offer in writing that is acceptable
 - Homeowner has right to reject offer
 - And no fee will be charged
- Various disclosures included in initial contact and throughout process [Regulation 0, 12 CFR 1015.2(a) and 1015.5(a)(b)(c)(1)(i-vii)(2)(d)(1)(2)]
 - Must be in writing
 - Designed to protect the homeowner
 - Must describe all material differences between the terms of the offer and the customer's current lender
 - Homeowner has the right to stop doing business with the provider at any time
 - No fee will be involved
 - False or misleading claims are prohibited in advertising or communication about services or performance
 - If homeowner is advised not to pay their mortgage, homeowner must also be made aware that this may damage their credit rating
 - And they could lose their home

Privacy Rules and Safeguard Rules and the Gramm-Leach-Bliley Act - GLBA

History of GLBA

The Glass-Steagall Act was formed in 1933 as a result of the financial failures due to the Great Depression. This act prohibited national and state banks from any affiliation with securities companies. In the mid-fifties, Congress passed the Bank Holding Company Act, this prohibited a bank from controlling a non-bank company; it was amended in 1982 forbidding banks from conducting general insurance underwriting or agency activities.

The Glass-Steagall Act was gradually undermined and eventually repealed in 1999 by the Financial Services Modernization Act, also called the Gramm-Leach-Bliley Act (GLBA). It is now legal for a holding company to have a bank, securities firm, and insurance company as subsidiaries.

With these mergers came privacy risks; some banks began selling consumer information with adverse consequences. Needless to say the consumers were concerned with how well they were protected against the sharing of their personal information.

Privacy protection under the Gramm-Leach-Bliley Act (GLBA) requires financial institutions to develop measures to protect the consumer's records and information. (Gramm-Leach-Bliley Act, 15 USC, Subchapter I Sec.6801-6809, Disclosure of Nonpublic Personal Information.)

Note: The GLBA requires financial institutions to protect information collected from individuals, this does not include business or commercial activities. GLBA, 15 USC §6801(a)(b)(1)(2)(3)

The GLBA permits the disclosure of consumer's information to credit reporting agencies, financial regulatory agencies as part of the sale of a business, to comply with any other laws or regulations, or as necessary for a transaction requested by the consumer.

The consumer must be provided with the following: [GLBA, 15 USC §6803(a)(1)(2)(3)(b)(c)(1)(A)(B)(2)(3)(4)]

- An initial (or "short-form") notice about the availability of the privacy policy if the financial institution shares information outside the permitted exceptions.
 - Privacy notice must be a clear, conspicuous, and accurate statement of the company's privacy practices.
 - Provide an opt-out notice, with the initial notice or separately, prior to a financial institution sharing nonpublic personal information with nonaffiliated third parties.
 - Consumers have the right to say "no" to having their information shared with a third party [GLBA, 15 USC §6802 (b)(1)(A)(B)(C)]
 - Provide consumers with a "reasonable opportunity" to opt out before disclosing nonpublic personal information about them to nonaffiliated third parties, such as 30 days from the date the notice is mailed.
 - If a consumer elects to opt out of all or certain disclosures, a financial institution must honor that opt-out direction as soon as is reasonably practicable after the opt-out is received.

The GLBA is composed of several parts; we will discuss two of those parts in this section:

- The Privacy Rule (Title 16 CFR 313)
- The Safeguards Rule (Title 16 CFR 314)

The definition of a "customer" is a consumer who has a "customer relationship" with a financial institution. A "customer relationship" is a continuing relationship with a consumer. [GLBA, Title 16, §313.4 (a)(1)]

The Gramm-Leach-Bliley (GLB) Act requires financial institutions to ensure the security and confidentiality of information on consumer's personal information. . [GLBA, Title 16, §314.1 (b)]

- Personal information includes:
 - Name
 - Address
 - Phone Number
 - Bank account numbers
 - Credit card numbers
 - Income
 - Credit History
 - Social Security number

The Federal Trade Commission (FTC) implemented the Gramm-Leach-Bliley Act and issued the Safeguards Rule requiring financial institutions to have measures in place to keep their customer information secure.

- Definition of financial institution: Any institution where the business of which is engaging in financial activities as described in section 4(k) of the Bank Holding Company Act (Title 12 USC §1843(k) and § 6809 (3)(A))
- Under the Final Rule promulgated by the Federal Trade Commission (FTC), an institution must be significantly engaged in financial activities to be considered a "financial institution."
 - Significantly engaged in financial activities includes, but is not limited to:
 - Check-cashing businesses
 - Pay-day lender
 - Mortgage brokers
 - Non-bank lenders
 - Credit counseling services and other financial advisors
 - A retailer that issues its own credit card
 - Auto dealers that lease and/or finance
 - Collection agency services
 - Relocation services that assists individuals with financing for moving expenses and/or mortgages
 - Sale of money orders, savings bonds, or traveler's checks
 - Real estate appraisers

To be in compliance a company must develop a written information security plan describing their customer information protection programs. Each company must: [GLBA, Title 16, 314.3 (a) and 314.4(a)(b)(1)(2)(3)(c)(d)(1)(2)e]

- Designate one or more employees to coordinate its information regarding their security program
- Identify and assess the risks to customer information in each relevant area of the company's operation, and evaluate the effectiveness of the current safeguards for controlling these risks
- Design and implement a safeguards program, and regularly monitor and test it
- Select service providers that can maintain appropriate safeguards, make sure your contract requires them to maintain safeguards, and oversee their handling of customer information
- Evaluate and adjust the program in light of relevant circumstances, including changes in the firm's business or operations, or the results of security testing and monitoring

Bank Secrecy Act also known as the Anti-Money Laundering (BSA/AML)

FDIC Law, Regulations, Related Acts - 8000-Miscellaneous Statutes and Regulations, Title 31-Money and Finance, Subtitle IV - Money, Chapter 5-Monetary Transactions, Subchapter II-Records on Monetary Instruments Transactions

The Bank Secrecy Act, also known as the Anti-Money Laundering Act, requires financial institutions to assist U.S. government agencies to detect and prevent money laundering.

The FDIC has this definition for money laundering: Money Laundering involves transactions intended to disguise the true source of funds; disguise the ultimate disposition of the funds; eliminate any audit trail and make it appear as though the funds came through legitimate sources; and evade income taxes.

- Financial institutions must:
 - Keep records of cash purchases of negotiable instruments [Title 31, CFR, Subpart C §1010.310]
 - File reports of cash purchases exceeding \$10,000 a day [Title 31, CFR, Subpart C §1010.311 and §1010.410 (all), Subpart D §1020.310]
 - Report suspicious activity that might signify money laundering, tax evasion, or other criminal activities [Title 31, CFR, Subpart C §1010.320 and Subpart C, §1012.320 (a)(1)(b)(1)(2)(i)(ii)(iii)(b)(1)(2)(3)]
- Types of transactions affected:
 - A Currency Transaction Report (CTR) must be used to report cash transactions in excess of \$10,000 during the same business day. An amount over \$10,000 can be either in one transaction or a combination thereof [Title 31, CFR, Subpart C §1010.310 through §1010.314 and §1010.330 (all)]
 - The Monetary Instrument Log (MIL) must indicate cash purchases of monetary instruments in value totaling \$3,000 - \$10,000, such as: [Title 31, CFR, Subpart D §1010.415 (all)]
 - Money orders
 - Cashier's checks
 - Traveler's checks
 - The MIL is required to be kept on record at the financial institution and readily available for an examiner's review

- The Suspicious Activity Report (SAR) will report any cash transaction where the customer appears to be avoiding the Bank Secrecy Act (BSA) reporting. The SAR is also used if the customer's actions suggest they are: [Title 31, CFR, Subpart C §1010.320 and Subpart C, §1012.320 (a) (1)(b)(1)(2)(i)(ii)(iii)(b)(1)(2)(3)]
 - Laundering money
 - Violating federal criminal laws
 - Committing wire transfer fraud
 - Committing check fraud
 - Involved in mysterious disappearances
- NOTE: The customer is not to have knowledge of the SAR being filed.

Authorities are usually not concerned with one CTR being filed for a consumer's account; although multiple CTR's from different institutions suggest suspicious activity.

STAY ON TRACK I

Upon completion of this lesson, you will

- Have a refresher course regarding the current Truth in Lending Act's current procedures and become familiar with the new disclosure process and forms
- Understand the Home Mortgage Disclosure Act and necessary forms
- Recognize the Real Estate Settlement Procedures Act and documentation required

In the following sections, “CFR” stands for “Code of Federal Regulations” and “USC” stands for “United States Code”. Once Congress passes a law it is recorded in the United States Code (USC) books, but it usually will not explain what procedures should be followed. The Code of Federal Regulations (CFR) explains how the laws are to be implemented.

Truth In Lending Act – REG Z

Consumer Protection Laws

- Consumer protection laws that apply to mortgage loan transactions:
 - Truth in Lending Act (TILA) [Bureau of Consumer Financial Protection – 12 CFR Chapter X, Part 1026 – Truth in Lending – Regulation Z]
 - Home Ownership and Equity Protection Act (HOEPA) [Section 32]
 - Real Estate Settlement Procedures Act (RESPA) [FDIC Law, Regulations, Related Acts, 6500 – Consumer Protection, Part 1024 – Real Estate Settlement Procedures, RESPA, Regulation X, 12 CFR, Part 1024]
- Truth in Lending Act (TILA) of 1968 is implemented by Federal Reserve Board's Regulation Z
 - Regulates disclosure of finance charges
 - Shows the estimated total costs of borrowing, the expected payment amounts over the life of the loan, and other significant loan features
- The Truth in Lending Act has as its stated purpose: Regulation Z, 12 CFR §1026.1(b)
 - *"The purpose of this part is to promote the informed use of consumer credit by requiring disclosures about its terms and cost. The regulation also includes substantive protections. It gives consumers the right to cancel certain credit transactions that involve a lien on a consumer's principal dwelling, regulates certain credit card practices, and provides a means for fair and timely resolution of credit billing disputes. The regulation does not generally govern charges for consumer credit, except that several provisions in Subpart G set forth special rules addressing certain charges applicable to credit card accounts under an open-end (not home-secured) consumer credit plan. The regulation requires a maximum interest rate to be stated in variable-rate contracts secured by the consumer's dwelling. It also imposes limitations on home-equity plans that are subject to the requirements of §1026.40 and mortgages that are subject to the requirements of §1026.32. The regulation prohibits certain acts or practices in connection with credit secured by a dwelling in §1026.36, and credit secured by a consumer's principal dwelling in §1026.35. The regulation also regulates certain practices of creditors who extend private education loans as defined in §1026.46(b)(5)."*

- All creditors must follow the same guidelines when disclosing certain charges and rates to consumers.
- It also ensures all creditors will use the same format when revealing these items in relation to the credit offer.
- Gives creditors the right to cancel certain credit transactions
- Requires a maximum interest rate stated on variable-rate transactions secured by a consumer's dwelling
- Imposes limits regarding certain home equity plans
- Prohibits certain acts or practices for credit secured by a dwelling
- Pertains to certain practices of creditors for private education loans

Truth in Lending Act

- The Truth in Lending Act it was created to put into practice the Truth in Lending and Fair Credit Billing Acts
- Requires documents that will provide consumers with pertinent information regarding their credit transaction
- The Truth in Lending Act allows the consumers to cancel a credit transaction if it includes a lien on their principal property
- The application of this regulation, by an individual or business entity, should be adhered to when the following conditions are met; Regulation Z, 12 CFR §1026.1 (c)(1)
 - When offering or extending credit to consumers Regulation Z, 12 CFR §1026.1 (c)(1)(i)
 - The service of offering or extending credit is done on a regular basis [Regulation Z, 12 CFR §1026.1 (c)(1)(ii)]
 - If a finance charge is attached to this credit or is payable in more than four monthly installments as per a written agreement [Regulation Z, 12 CFR §1026.1 (c)(1)(iii)]
 - The use of this credit will be primarily for personal, family, or household purposes [Regulation Z, 12 CFR §1026.1 (c)(1)(iv)]
- The Truth in Lending Act contains rules for open-end and closed end credit transactions [Regulation Z, 12 CFR Subpart B – Open End Credit and Subpart C Closed End Credit]
- Open-end credit involves the consumer being given credit in which creditor reasonably contemplates repeated transactions [Regulation Z, 12 CFR §1026.2 (a)(20)(i)]
- The creditor may impose a finance charge from time to time on an outstanding unpaid balance [Regulation Z, 12 CFR §1026.2 (a)(20)(ii)]
- The amount of credit limited by the creditor may be extended to the consumer during the term of the plan [Regulation Z, 12 CFR §1026.2 (a)(20)(iii)]
- This is generally made available to the extent that any outstanding balance is repaid [Regulation Z, 12 CFR §1026.2 (a)(20)(iii)]
- Examples of open-end credit would be
 - Bank credit cards
 - Home Equity Lines of Credit (HELOC)
 - Department store or service station credit cards
 - Overdraft privileges
- Closed-end credit involves all other transactions, such as, car loans or mortgages [Regulation Z, 12 CFR §1026.2 (a)(10)]
- One objective of the Truth in Lending Act is to require the mortgage originator to disclose to the consumer their interest rate reflected as an annual percentage rate (APR), showing [Regulation Z, 12 CFR §1026.22 (a)]
 - The cost of credit, within three business days of application [Regulation Z, 12 CFR §1026.19 (a)]
 - Pre-Paid finance charge and what it includes [Regulation Z, 12 CFR §1026.4 (a)]
 - How it was used to calculate the annual percentage rate
- Truth In Lending Act applies to any mortgage loan used for personal, family, or household purposes such as:
 - Buying/remodeling a home
 - Consolidating personal debt
 - Sending kids to college
- Truth In Lending Act only applies to loans made to natural persons [Regulation Z, 12 CFR §1026.2 (a)(11)]
 - TILA doesn't apply to:
 - Loans made to corporations or organizations [Regulation Z, 12 CFR §1026.3 (a)]
 - Loans made for business, commercial, or agricultural purposes [Regulation Z, 12 CFR §1026.3 (a)(1)]
 - Most seller financing is also exempt
- TILA's disclosure requirements apply to lenders and credit arrangers (including mortgage brokers)
 - Must give applicant disclosure statement with estimates of loan costs within 3 business days of receiving consumer's written application [Regulation Z, 12 CFR §1026.19 (a)]
- Mortgage Disclosure Improvement Act – MDIA
 - Housing Economic Recovery Act – HERA

- Includes amendments to Truth in Lending Act
 - Known as the Mortgage Disclosure Improvement Act – MDIA
 - Requires creditors to give consumers transaction-specific cost disclosures
 - For dwelling secured closed end mortgage transactions subject to Real Estate Settlement Procedures Act (RESPA)
 - Even though it is not the consumer’s principal dwelling (place of residence)
- Early disclosures now cover more transaction types [Regulation Z, 12 CFR §1026.19 (a)(1)(i)]:
 - Purchase a home
 - Principal dwelling or second home
 - Construct a home
 - Refinance a home
 - Second mortgages
 - Home equity loans
 - Does not include HELOC
 - These have different disclosure requirements
- Before MDIA:
 - TILA, Regulation Z, 12 CFR Section 128 (b)(2) applied only to a “residential mortgage transaction” subject to RESPA
- Now:
 - Extends early disclosure requirement to “any extension of credit secured by the dwelling of a consumer” [Regulation Z, 12 CFR §1026.19 (a)(1)(i)]
 - Now includes refinance and home equity loans
- For all applications received after July 30, 2009
 - Initial fee restrictions prior to the issuance of early disclosures [Regulation Z, 12 CFR §1026.19 (a)(1)(iii)]
 - No upfront fees except for reasonable credit report fee
 - Notice must be clear and conspicuous [Regulation Z, 12 CFR §1026.19 (a)(4)]
 - *“You are not required to complete this agreement merely because you have received these disclosures or signed a loan application”*
 - Pertains to initial and corrected disclosures
- Timing for disclosures
 - Initial disclosure [Regulation Z, 12 CFR §1026.19 (a)(1)(i)]
 - Delivered or placed in the mail not later than 3 business days after:
 - Receipt of the loan application
 - Business day defined for initial disclosures [Regulation Z, 12 CFR §1026.2 (a)(6)]
 - Days in which creditor is open for business
- Waiting period prior to consummation [Regulation Z, 12 CFR §1026.19 (a)(2)]
 - 7 business days from delivery of initial disclosures
- Business day defined for “new” waiting period [Regulation Z, 12 CFR §1026.2 (a)(6)]
 - All calendar days except for Sundays and legal holidays
- APR Tolerance Levels
 - Regular Transactions (Regulation Z, 12 CFR §1026.22 (a)(2))
 - APR is considered accurate if it varies by not more than 1/8 of 1 percentage point
 - Example: Exact APR is 10 1/8%
 - A disclosed APR from 10% - 10 1/4% is in compliance with this regulation
- Irregular Transactions (Regulation Z, 12 CFR §1026.22 (a)(3))
 - APR is considered accurate if it varies by not more than 1/4 of 1 percentage point
 - Examples of an irregular transaction could be:
 - More complex transactions that do not call for a single advance and a regular series of equal payments at equal intervals
 - Construction loan with advances as construction progresses
 - Transactions where payments vary with consumer’s seasonal income
 - Graduated payment schedules
 - Does not apply to loans with variable rate features where initial disclosures are based on a regular amortization schedule
 - Even though payments may later change because of the variable rate feature
- If APR changes beyond allowed tolerance [Regulation Z, 12 CFR §1026.19 (a)(2)(ii)]
 - Regular Transactions-1/8 of 1 percentage point
 - Irregular Transactions-1/4 of 1 percentage point

- Corrected disclosure received by consumer on or before third business day before consummation
 - Business day defined [Regulation Z, 12 CFR §1026.2 (a)(6)]
 - Different from initial disclosures
 - All calendar days except Sundays and legal holidays
 - “3-7-3 Rule” of Mortgage Disclosure Improvement Act
- RESPA defines tolerance:
 - *“Tolerance means the maximum amount by which the charge for a category or categories of settlement costs may exceed the amount of the estimate for such category or categories on a GFE.” [Regulation Z, 12 CFR §1024.2]*
- RESPA defines changed circumstances:
 - Changed circumstances means: [Regulation Z, 12 CFR §1024.2 (b)(1)]
 - Acts of God, war, disaster, or other emergency;
 - Information particular to the borrower or transaction that was relied on in providing the GFE and that changes or is found to be inaccurate after the GFE has been provided. This may include information about the credit quality of the borrower, the amount of the loan, the estimated value of the property, or any other information that was used in providing the GFE;
 - New information particular to the borrower or transaction that was not relied on in providing the GFE; or
 - Other circumstances that are particular to the borrower or transaction, including boundary disputes, the need for flood insurance, or environmental problems.
- “No Requirement to Complete Statement” Notice [Regulation Z, 12 CFR §1026.19 (a)(4)]
 - Disclosures and corrected disclosures must contain a notice
 - “You are not required to complete this agreement merely because you have received these disclosures or signed a loan application”
 - Must be clear and conspicuous

SUNDAY	MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY	SATURDAY
	1 Loan Application is taken, Disclosures Delivered in Person or Disclosures Mailed disclosures provided during face-to-face application are considered delivered that day – not on the 3rd day. Fees may be collected	2 DAY 1	3 DAY 2	4 DAY 3 Considered Received By Borrower... *Can Collect Additional Fees	5 DAY 4	6 DAY 5
7	8 DAY 6	9 DAY 7 Earliest Loan Can Close	10	11	12	13
14	15 Loan Is Approved, New Rate Quoted & APR Increased By .125	16 New Disclosures Signed and Dated By Borrower In Your Office	17 DAY 1	18 DAY 2	19 DAY 3 Loan May Close & Fund	20

- Waiver of 7 and 3-day waiting period [Regulation Z, 12 CFR §1026.19 (a)(3)]
 - Consumer can expedite consummation for bona fide personal emergency
 - Consumer prepares a handwritten statement that:
 - Specifically describes details of emergency
 - Specifies request for waiver of the waiting period
 - Is dated
 - Is signed by each consumer
- Protection for Higher-Priced Mortgage Loans [Regulation Z, 12 CFR §1026.35 (a)]
 - To prevent unfairness, deception and abuse on higher priced mortgage loans
 - Consumer-purpose loans
 - Closed-end loans
 - Secured by consumer's principal dwelling
 - Having an APR that exceeds average prime by at least
 - 1.5 % points for first-lien loans
 - 3.5% points for subordinate-lien loans
- Creditors are prohibited from extending credit without regard to a consumer's ability to repay from sources other than the collateral itself [Regulation Z, 12 CFR §1026.35 (b) (1)]
- Creditors must verify income and assets relied upon in determining repayment ability
- Creditors must establish escrow accounts for taxes and insurance [Regulation Z, 12 CFR §1026.35 (3)(i)]
 - Borrowers may cancel escrows 12 months after consummation of loan [Regulation Z, 12 CFR §1026.35 (3)(iii)]
- Creditors are prohibited from structuring closed-end mortgage loans as open-end lines of credit for the purpose of evading these rules [Regulation Z, 12 CFR §1026.35 (4)]
- Mortgage Disclosure Improvement Act (MDIA) seeks to alert borrowers to risks of payment increases
 - Before loans with variable rates/payments are made
- The Truth in Lending Act was created to ensure the same format is used when disclosing
 - Rates
 - Terms
 - Charges

Advertising rules

Intended to “protect consumers from unfair or deceptive home mortgage lending and advertising practices”
 The advertising rules prohibit the following practices which could be misleading:

- Advertising a “fixed” rate when this rate is fixed for a limited time period and not the loans full term [Regulation Z, 12 CFR §1026.24 (1)(i)(A)(B)(ii)(iii)(A)(B)]
- Using a comparison model demonstrating a hypothetical consumer's current rate or payment obligations to the advertised product, unless the advertisement states the rates or payments over the life of the loan [Regulation Z, 12 CFR §1026.24 (i)(2)(i)(ii)]
- Advertisements that characterize the products offered as “government loan programs”, “government-supported or sponsored loans” unless it is a government type loan such as FHA or VA or similar loan [Regulation Z, 12 CFR §1026.24 (i)(3)]
- Advertisement such as flyers, solicitation letters, etc., that display the name of the consumer's current lender, unless it is prominently disclosed on the advertisement that the mortgage lender is not affiliated with the consumer's current lender [Regulation Z, 12 CFR §1026.24 (i)(4)(i)(ii)]
- Advertisements that make claims of debt elimination if the advertised product will only be replacing one debt obligation with another [Regulation Z, 12 CFR §1026.24 (i)(5)]
- Advertisements that falsely create the impression that the mortgage broker or lender has a “counselor” relationship with the consumer [Regulation Z, 12 CFR §1026.24 (i)(6)]
- Foreign-language advertisements in which certain information such as a low introductory “teaser” rate, is provided in a foreign language, while required disclosures are provided only in English in the same advertisement [Regulation Z, 12 CFR §1026.24 (i)(7)]

Highlights of Final Rules on Loan Originator Compensation and Steering

- To protect mortgage borrowers from unfair, abusive, or deceptive practices arising from originator compensation practices

- New rules apply to those who originate loans
 - Mortgage brokers and companies that employ them
 - Mortgage loan originators employed by depository institutions
 - Other lenders
- Final rules apply to
 - Closed-end loans
 - Secured by consumer's dwelling
- Final rule prohibits
 - Payment to the loan originator based on the loan's interest rate or other terms
 - Compensation based on a fixed % of the loan amount is allowed
 - A mortgage broker or loan originator from receiving payments directly from a consumer while also receiving compensation from the creditor or another person
 - A mortgage broker or loan originator from "steering" a consumer to a lender offering less favorable terms to enable the broker or loan originator's compensation to increase
- Final rule will provide
 - A safe harbor to facilitate compliance with the anti-steering rule
- Safe harbor is met if:
 - The consumer is presented with loan offers for each type transaction they are interested in
 - Fixed rate, ARM or reverse mortgage
 - Loan options presented to the consumer will include the following:
 - Lowest interest rate consumer qualifies for
 - Lowest points and origination fees
 - Lowest rate for which the consumer qualifies for a loan with no risky features, such as:
 - Prepayment penalty
 - Negative amortization
 - Balloon payment in the first 7 years
- Definition of loan originator: [Regulation Z, 12 CFR §1026.36 (a)(1)(i)]
"For purposes of this section, the term "loan originator" means a person who, in expectation of direct or indirect compensation or other monetary gain or for direct or indirect compensation or other monetary gain, performs any of the following activities: takes an application, offers, arranges, assists a consumer in obtaining or applying to obtain, negotiates, or otherwise obtains or makes an extension of consumer credit for another person; or through advertising or other means of communication represents to the public that such person can or will perform any of these activities. The term "loan originator" includes an employee, agent, or contractor of the creditor or loan originator organization if the employee, agent, or contractor meets this definition. The term "loan originator" includes a creditor that engages in loan origination activities if the creditor does not finance the transaction at consummation out of the creditor's own resources, including by drawing on a bona fide warehouse line of credit or out of deposits held by the creditor. All creditors that engage in any of the foregoing loan origination activities are loan originators for purposes of paragraphs (f) and (g) of this section."

Mortgage Loan Originator (MLO) Qualification and Compensation Practices [Regulation Z, 12 CFR §1026.36 (all)]

- Applies to all MLOs and the organizations which employ them
 - MLOs cannot be compensated for the following on the mortgage loan:
 - Interest rate
 - Yield Spread Premium (YSP)
 - Sale of services
 - Example: Title Insurance from an affiliate
 - Cannot steer consumer into any transaction resulting in more compensation for the MLO
 - Unless the transaction will benefit the consumer
 - Proxy for a term of a transaction
 - Example: Steering a consumer into a loan which would pay the MLO a higher commission
- MLOs are allowed to be compensated for:
 - Salary
 - Commission that is based on dollar volume or number of loans closed
 - Participation in 401(k), ESOP, bonus, or retirement plans

- Also prohibits "dual compensation"
 - This occurs when a loan originator receives compensation from the consumer and an additional party other than the originator's organization
 - Exception - Allows a loan originator organization to pay its employees or contractors a commission provided that commission is not based on a term of a loan
- Pricing Concessions
 - MLO's may decrease their compensation to assist the borrower if:
 - An unforeseen increase or actual settlement cost which exceeded the estimated cost disclosed
 - An unforeseen settlement cost not previously disclosed
- MLO Qualifications and Identification
 - MLOs must:
 - Be licensed or registered under the provisions of the Secure and Fair Enforcement for Mortgage Licensing Act
 - Also known as S.A.F.E. and SAFE Act
 - Place their name and NMLS unique identifier number on loan documents
 - Be subject to a full background check
 - Receive ongoing continuing education instruction
- Record Keeping
 - Community banks must:
 - Keep records of all compensation paid to MLOs for three years after date paid
 - Keep records of compensation paid to them by other creditors for up to three years after compensation is paid
- Record keeping also includes keeping:
 - Copies of individual compensation plans for MLOs for three years
 - Written policies and procedures for:
 - Mortgage loan compensation programs
 - Screening and background checks used in hiring MLOs
 - Records pertaining to registration and licensing of MLOs with the NMLS
- [Regulation Z, 12 CFR §1026.36(h)]
 - Creditors cannot force borrowers into contracts requiring mandatory arbitration
 - Prohibits the financing fees and premiums from single premium credit
 - Examples: Credit life, disability, unemployment

Real Estate Settlement Procedures Act (RESPA) [FDIC Law, Regulations, Related Acts, 6500 – Consumer Protection, Part 1024 – Real Estate Settlement Procedures, RESPA, Regulation X, 12 CFR, Part 1024]

- Real Estate Settlement Procedures Act (RESPA), passed in 1974
- RESPA has two main goals:
 - To provide borrowers with information about closing costs
 - To eliminate kickbacks and referral fees that unnecessarily increase settlement costs
- The purpose of RESPA of 1974 – REG X
 - Essentially the Real Estate Settlement Procedures Act is divided into two groupings
 - One section manages disclosures and servicing requirements for transactions involving a "federally related residential loan"
 - The second set prohibits the payment or receipts of fees from the borrower that were not actually earned
 - The payment or receipt of unearned fees (fee-splitting) or referral fees are prohibited for anyone, not just borrower [Regulation X, 12 CFR §1024.14 (a)(b)]
- RESPA ensures the consumer receives certain disclosures in a timely manner
 - Disclosures should:
 - Detail the costs associated with each loan transaction
 - Provide information on lender servicing and escrow account practices
 - Describe business relationships between settlement providers
- The Real Estate Settlement Procedures Act involves [Regulation X, 12 CFR §1024.2 (b) (Under "Federally Related Mortgage Loan or Mortgage Loan means as follows")]
 - One-to-four family residential property
 - Which includes most loans secured by a lien (first or subordinate position).

- Included in this grouping are [Regulation X, 12 CFR §1024.2 (b) (Under “Federally Related Mortgage Loan or Mortgage Loan means as follows”)]
 - Purchase loans
 - Assumptions
 - Refinances
 - Property improvement loans
 - Equity lines of credit
 - Reverse mortgages

RESPA Covered Transactions

- RESPA applies to “federally related” loan transactions. Loan is federally related if [Regulation X, 12 CFR §1024.2 (b)(1) (all) (Under “Federally Related Mortgage Loan or Mortgage Loan means as follows”)] :
 - It is secured by a mortgage or deed of trust against:
 - Property with (or loan funds will be used to build) dwelling of four units or less;
 - Condominium unit or cooperative apartment; or
 - Lot with mobile home;

AND
 - Lender is federally regulated, has federally insured accounts, is assisted by federal government, makes loans in connection with federal program, sells loans to Fannie Mae, Ginnie Mae, or Freddie Mac, or makes real estate loans that total more than \$1,000,000 per year
 - Basically any loan other than temporary financing
 - And exemptions in next section

RESPA Exemptions

- RESPA doesn't apply to loans [Regulation X, 12 CFR §1024.5 (a)(b)]:
 - To purchase 25 acres or more
 - Primarily for business, commercial, or agricultural purpose
 - To vacant land
 - Unless within two years from the date of the settlement of the loan, a structure or a manufactured home will be constructed or placed on the real property using the loan proceeds
 - Temporary financing (construction loan)
 - Assumption without lender approval
- RESPA has certain requirements for federally related loan transactions
- Lender must give applicants within 3 days of written loan application:
 - Booklet about settlement procedures [Regulation X, 12 CFR §1024.6 (all)]
 - Loan Estimate [Regulation Z, 12 CFR §1026.19(e)(1)(iii)]
 - Mortgage servicing disclosure statement [Regulation X, 12 CFR §2605 (All)]
- Closing agent must itemize loan settlement charges on Uniform Settlement Statement form [Regulation X, 12 CFR §1024.8 (b)(1)]
- If borrower required to make deposits into impound account, lender can't require excessive deposits [Regulation X, 12 CFR §1024.17 (a)]
- Lender or provider of settlement services may not:
 - Pay kickbacks or referral fees [Regulation X, 12 CFR §1024.14 (b)]
 - Accept unearned fees [Regulation X, 12 CFR §1024.14 (c)]
 - Charge a document preparation fee
- Property seller may not require buyer to use a particular title company [Regulation X, 12 CFR §1024.14 (f)(2)]

RESPA – Definitions [Regulation X, 12 CFR §1024.2 (b)]

Origination service means any service involved in the creation of a mortgage loan, including but not limited to the taking of the loan application, loan processing, and the underwriting and funding of the loan, and the processing and administrative services required to perform these functions.

Mortgage broker means a person (not an employee of a lender) or entity that renders origination services and serves as an intermediary between a borrower and a lender in a transaction involving a federally related mortgage loan, including such a person or entity that closes the loan in its own name in a table funded transaction. A loan correspondent approved under 24 CFR 202.8 for Federal Housing Administration programs is a mortgage broker for purposes of this part.

Loan originator means a lender or mortgage broker.

Third party means a settlement service provider other than a loan originator.

Title service means any service involved in the provision of title insurance (lender's or owner's policy), including but not limited to: title examination and evaluation; preparation and issuance of title commitment; clearance of underwriting objections; preparation and issuance of a title insurance policy or policies; and the processing and administrative services required to perform these functions. The term also includes the service of conducting a settlement.

Disclosures Required at Loan Application

- HUD's Settlement Cost Booklet [Regulation X, 12 CFR §1024.6 (a)(1)]
- Must be used with GFE [Regulation X, 12 CFR §1024.7] and HUD-1 [Regulation X, 12 CFR §1024.8]
 - The Secretary of (HUD) prepares and distributes these special information booklets
 - The booklet enables the consumer to better understand the purpose and expenses involved in a real estate transaction
 - Purchase transactions only [Regulation X, 12 CFR §1024.6 (a)]
 - The Secretary of HUD shall prescribe the form used for each booklet [Regulation X, 12 CFR §1024.6 (c)]
- The Special Information Booklet goes on to explain:
 - The nature and purpose of escrow accounts
 - Choices available when selecting persons to provide necessary services
 - An explanation of the unfair practices and unreasonable or unnecessary charges to be avoided by the consumer
- The HUD Special Information Booklet should be delivered or placed in the mail to the borrower [Regulation X, 12 CFR §1024.6 (a)(1)]
 - Not later than three business days after the application is rec'd or prepared
 - Two or more persons apply, only one person needs to be given booklet
 - If mortgage broker is used, they may deliver booklet
 - Intent is to ensure booklet is rec'd at earliest possible date
- The HUD Special Information Booklet does not need to be provided for [Regulation X, 12 CFR §1024.6 (a)(3)]:
 - Refinancing transactions;
 - Closed end loans with subordinate lien;
 - Reverse mortgages;
 - Any federally related mortgage whose purpose is not to purchase a 1 – 4 family residential property.
- Every applicant is given a "Servicing Disclosure Statement" at application
- This format was effective January 16, 2009
 - Located under RESPA – Appendix MS-1 to Part 1024
 - Reveals mortgage loan payments may be transferred
 - Defines "Servicing"

Disclosures Required Before Settlement/Closing Occurs

- Affiliated Business Arrangement (AfBA) Disclosure [Regulation X, 12 CFR §1024.15 (All)]
 - Required whenever a settlement provider refers the consumer to a provider with whom the referring party has an ownership or other beneficial interest [Regulation X, 12 CFR §1024.15 (b)(1)]
 - Necessary whenever a transaction involves a RESPA covered transaction.
 - The referring party is responsible for providing the Affiliated Business Arrangement Disclosure to the consumer either at or prior to the time of the referral [Regulation X, 12 CFR §1024.15 (b)(1)]
 - Gives a description of the business affiliation between the two parties [Regulation X, 12 CFR §1024.15 (b)(1)]
 - An estimate of the second provider's charges [Regulation X, 12 CFR §1024.15 (b)(1)]
 - Sample located in RESPA under Appendix D
- Initial Escrow Statement [Regulation X, 12 CFR §1024.17]
 - Monthly collection the lender receives from the borrower for property taxes and insurance premiums
 - Submitted at closing or within 45 days of closing [Regulation X, 12 CFR §1024.17 (g)(i)(ii)]

- The “Initial Escrow Statement” reveals to the borrower an itemization of charges to be paid from the Escrow Account during the first twelve months of the loan. [Regulation X, 12 CFR §1024.17 (g)(i)(ii)]
 - Discloses
 - Escrow payment
 - Any additional funds (cushion) kept in the escrow account
 - Lender is obligated to deliver the Initial Escrow Statement 45 days from date of settlement

Disclosures After Settlement

- The loan servicer usually produces the following two documents:
 - The Annual Escrow Statement [Regulation X, 12 CFR §1024.17 (i)(1)(i–viii)(2)(3)(4)(i)(ii)(iii)(j)]
 - The Servicing Transfer Statement [Regulation X, 12 CFR §1024.21 (All)]
- Annual Escrow Statement
 - A summary, delivered to the borrower annually,
 - Lists deposits and payments made during the lenders or loan servicers twelve-month computation year
 - Notifies borrower of any shortages or overages in the account
 - What course should be taken to correct any discrepancies the account
- Servicing Transfer Agreement
 - It is common in the lending industry for a loan servicer to sell or assign the servicing rights of a borrower’s loan to another servicer
- The loan servicer must notify the borrower with a Servicing Transfer Statement
 - The current loan servicer has 15 days before the effective date of the loan transfer to notify the borrower
 - The borrowers new loan servicer has 15 days after the effective date of the loan transfer to notify the borrower of this action
- Information on the Servicing Transfer Statement will list:
 - The name and address of the new servicer
 - Toll-free numbers
 - The date the new servicer will begin accepting payment

Consumer Protections and Prohibited Practices

- Section 8 - Kickbacks, Fee Splitting, Unearned Fees [Regulation X, 12 CFR §1024.14]
 - Section 8 (a) of RESPA states, “No person shall give and no person shall accept any fee, kickback or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person.” [Regulation X, 12 CFR §1024.14 (a)(b)]
- Section 8 forbids anyone to accept or give a fee, kickback or anything of value in exchange for referrals
- Section 8 (b) states, “No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a real estate service in connection with a transaction involving a federally related mortgage loan other than for services actually performed.” [Regulation X, 12 CFR §1024.14 (c)]
- Example of Section 8 – Prohibited Practices
- Suppose a lender is offering a contest for appraisers, realtors, and attorneys where the person who sends the lender the most referrals for the month of March wins four free dinners for two at an area restaurant. This would not be allowed under RESPA since the dinner is considered a thing of value in exchange for the referral of business. Also, the fact the lender offered or gave an opportunity to win the dinners is considered a thing of value
- Alternatively the lender can offer to a borrower an incentive
 - Such as a chance to win the same dinner for two as long as the promotion is not based on the borrower referring business to the lender
- Promotional items from the lender, can be given to realtors, attorneys, etc., such as:
 - Ink pens
 - Post it note pads
 - Magnets
- Materials must be normal promotional items with the lenders information attached
- Lender may not purchase promotional items for an attorney, with that attorneys name on the items, for the attorney to use to market clients for real estate business
 - This is an item of value given for referral of loan business

- Section 8 (c) does not prohibit these practices [Regulation X, 12 CFR §1024.14]
 - An attorney is compensated for services performed [Regulation X, 12 CFR §1024.14 (g) (i)]
 - A title company is paid a fee to its appointed agent for services fulfilled in the issuance of a title insurance policy. [Regulation X, 12 CFR §1024.14 (g)(ii)]
 - A lender compensating its mortgage loan originator for services performed in the making of a loan [Regulation X, 12 CFR §1024.14 (g)(iii)]
 - As long as it's a bona fide payment to a person for services actually performed or salary or compensation for goods furnished [Regulation X, 12 CFR §1024.14 (g)(iv)]
- Section 9 – Title Companies [Regulation X, 12 CFR §1024.16 (All)]
 - It is a violation of Section 9 for the seller of a property to require the homebuyer to use a particular title company as a condition of the sale
 - If this provision is violated the seller shall be liable to the buyer in an amount equal to three times the charges for title insurance

RESPA Enforcements

- Violation of Section 8 [Regulation X, 12 CFR §1024.19 (All)]
 - Violations of Section 8's anti-kickback, referral fees, and unearned fees provisions of RESPA are subject to criminal and civil penalties
 - Section 8 (d) specifies anyone who violates this section shall be fined not more than \$10,000.00 or imprisonment for not more than one year, or both
 - It continues to state in a private lawsuit, a person who violates Section 8 may be liable to the person charged for the settlement service, an amount equal to three times the amount of the charge initially paid for the service
 - Any violations of Sections 8 or 9 have a one-year deadline for an individual to bring forth a private law suit

Escrow Accounts and RESPA

- An escrow account is;
 - A system that guarantees to the lender the taxes and insurance on the property will be paid
 - A non-interest bearing account designed for use in paying borrower's:
 - Annual taxes
 - Insurance
 - Any other charges related to the property
- The same method is performed for city and parish/county taxes
 - The lender will charge the borrower 1/12 of the total annual taxes and place this amount in the escrow account each month
 - At the end of the one-year period, funds are available to pay the taxes
- Lenders are allowed to maintain a "cushion" in the escrow account to make up for any shortages that may arise from increasing insurance costs or tax increases over the term of the loan
 - Cushion amount may not exceed 1/6 of the total disbursement for the year
 - Cushion amount is allowed but not a requirement of RESPA
- Escrow Analysis
 - An escrow analysis is to be performed annually by the lender
 - Any excess of \$50.00 or more over the cushion amount must be returned to the borrower
 - Any shortages in the escrow account must be disclosed to the borrower on this analysis
- Escrow Review
 - It is the individual lender's discretion to decide when and if an escrow account is required
 - HUD regulations only limit the maximum amount that a lender can require a borrower to maintain in an account
 - The Real Estate Settlement Procedures Act does not force lenders to require an escrow account for each borrower

Home Mortgage Disclosure Act - Regulation C 12 CFR, Part 1003

- Home Mortgage Disclosure Act (HMDA), helps government spot redlining and predatory lending
 - Pronounced Hum-Duh

- HMDA applies to:
- Financial institutions [Regulation C, 12 CFR §1003.2 (e)(1)(i)(ii)(iii)(iv)(A)(B)(C)]
 - For-profit mortgage lending institutions [Regulation C, 12 CFR §1003.2 (i)(ii)(iii)(A)(B)]
 - Lenders must submit annual report to government on residential mortgage loans
- HMDA has as its purpose:
 - *“This regulation implements the Home Mortgage Disclosure Act, which is intended to provide the public with loan data that can be used [Regulation C, 12 CFR §1003.1 (b)(1)]:*
 - *To help determine whether financial institutions are serving the housing needs of their communities [Regulation C, 12 CFR §1003.1 (b)(1)(i)]*
 - *To assist public officials in distributing public-sector investment so as to attract private investment to areas where it is needed [[Regulation C, 12 CFR §1003.1 (b)(1)(ii)]; and*
 - *To assist in identifying possible discriminatory lending patterns and enforcing antidiscrimination statutes. [Regulation C, 12 CFR § [1003.1 (b)(1)(iii)]*
 - *Neither this act nor this regulation is intended to encourage unsound lending practices or the allocation of credit.” [Regulation C, 12 CFR §1003.1 (b)(2)]*
- Financial institutions include:
- A bank, savings association, or credit union that [Regulation C, 12 CFR §1003.2 (e)(1)]
 - On preceding Dec. 31 had assets in excess of threshold set forth by the Board [Regulation C, 12 CFR §1003.2 (e)(1)(ii)]
 - On preceding Dec. 31, had a home or branch in a metropolitan area [Regulation C, 12 CFR §1003.2 (e)(1)(ii)]
 - In the preceding calendar year, originated at least one purchase or refinance loan [Regulation C, 12 CFR §1003.2 (e)(1)(iii)]
- Meets one or more of the following:
 - Institution is federally insured [Regulation C, 12 CFR §1003.2 (e)(1)(iv)(A)]
 - Mortgage loan was insured, guaranteed or supplemented by a federal agency [Regulation C, 12 CFR §1003.2 (e)(1)(B)]
 - The mortgage loan was intended for sale to FNMA or Freddie Mac [Regulation C, 12 CFR §1003.2 (e)(1)(C)]
- A for profit mortgage lending institution is:
 - In the preceding calendar year, either [Regulation C, 12 CFR §1003.2 (2)(i)]:
 - Originated home purchase loans that equal 10% of its loan origination volume [Regulation C, 12 CFR §1003.2 (2)(i)(A)]
 - Originated home purchase loans that equaled at \$25 million [Regulation C, 12 CFR §1003.2 (2)(i)(B)], and
 - Either:
 - On the preceding Dec. 31 had total assets of more than 10 million [Regulation C, 12 CFR §1003.2 (2)(iii)(A)]
 - In the preceding year originated at least 100 purchase loans [Regulation C, 12 CFR §1003.2 (2)(iii)(B)]
- Lender must also provide data for, and originations and purchases in each calendar year on [Regulation C, 12 CFR §1003.4 (a)]:
 - Home purchase loans
 - Home improvement loans
 - Refinances
- Data must be collected on requests under a preapproval program [Regulation C, 12 CFR §1003.4 (a)]
 - A request for preapproval is an application if a written commitment is issued to the applicant [Regulation C, 12 CFR §1003.2 (b)(2)]
- If preapproval results in a denial or origination of a loan, the data reported on the HMDA shall contain [Regulation C, 12 CFR §1003.4 (b)]:
 - An identifying number for the loan [Regulation C, 12 CFR §1003.4 (b)(1)]
 - The type of loan or application [Regulation C, 12 CFR §1003.4 (b)(2)]
 - The purpose of the loan [Regulation C, 12 CFR §1003.4 (b)(3)]
 - Reason for request and results [Regulation C, 12 CFR §1003.4 (b)(4)]
 - Property type [Regulation C, 12 CFR §1003.4 (b)(5)]
 - Occupancy status [Regulation C, 12 CFR §1003.4 (b)(6)]
 - Amount of loan [Regulation C, 12 CFR §1003.4 (b)(7)]
 - Action taken and date [Regulation C, 12 CFR §1003.4 (b)(8)]
 - Location of property [Regulation C, 12 CFR §1003.4 (b)(9)]

- Ethnicity, race and sex of applicant [Regulation C, 12 CFR §1003.4 (b)(10)]
- Entity purchasing loan [Regulation C, 12 CFR §1003.4 (b)(11)]
- Difference between loan's APR and the yield on Treasury securities [Regulation C, 12 CFR §1003.4 (b)(12)]
- This information allows the federal government to:
 - Monitor lending patterns and analyze them for any evidence of illegal discrimination [Regulation C, 12 CFR §1003.1 (b)(1)(iii)]
- This information is collected on a Home Mortgage Disclosure Act report or HMDA Depository and non-depository institutions that meet certain reporting criteria must complete a HMDA Loan Application Register (LAR) [Regulation C, 12 CFR §Appendix A to Part 1003]
 - Contains information from applications for home purchases, refinances, and home improvement loans [Regulation C, 12 CFR §1003.4 (a)]
 - Data submitted on the HMDA Loan Application Register is used by the Federal Financial Institutions Examination Council (FFIEC) to create reports for each metropolitan area (MA)
 - These reports are available to the public at central data depositories located in each metropolitan area [Regulation C, 12 CFR §1003.5 (b)(2)]
- To comply with the Home Mortgage Disclosure Act:
 - First determine if the loan fits into one of the previously listed categories
 - If the loan is HMDA reportable government monitoring information on the loan application must be read or shown to the applicants [Regulation C, 12 CFR Appendix B to Part 1003 – II A, B, C, and D]
 - If they choose not to disclose the information, the mortgage loan originator must make a visual observation
- If a telephone, mail, or internet application takes place [Regulation C, 12 CFR §Appendix A to Part 1003 – I D 2]:
 - The mortgage loan originator is still required to determine if HMDA applies
 - You must ask the applicant for this information, but you cannot require the applicant to provide it
 - Inform applicant, reason for information is to prohibit discrimination
 - If applicant declines to provide information, the data need not be provided
 - If this is the case, indicate how application received
 - Mail, telephone or Internet

STAY ON TRACK II - TRID

Upon completion of this lesson you should be able to:

- Understand the different sections of the new integrated forms; the Loan Estimate and the Closing Disclosure
- Realize the benefits of these new forms
- Know which type of mortgages will be covered by the new disclosure rules

Introduction

- For more than 30 years, Federal law has required lenders to provide two different disclosure forms to consumers applying for a mortgage. The law also has generally required two different forms at or shortly before closing on the loan. Two different Federal agencies developed these forms separately, under two Federal statutes: the Truth in Lending Act (TILA) and the Real Estate Settlement Procedures Act of 1974 (RESPA). The information on these forms is overlapping and the language is inconsistent. Not surprisingly, consumers often find the forms confusing. It is also not surprising that lenders and settlement agents find the forms burdensome to provide and explain.
- The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) directs the Consumer Financial Protection Bureau (the Bureau) to integrate the mortgage loan disclosures under TILA and RESPA sections 4 and 5. Section 1032(f) of the Dodd-Frank Act mandated that the Bureau propose for public comment rules and model disclosures that integrate the TILA and RESPA disclosures by July 21, 2012. The Bureau satisfied this statutory mandate and issued proposed rules and forms on July 9, 2012.

- To accomplish this, the Bureau engaged in extensive consumer and industry research, analysis of public comment, and public outreach for more than a year. After issuing the proposal, the Bureau conducted a largescale quantitative study of its integrated disclosures with approximately 850 consumers, which concluded that the Bureau's integrated disclosures had on average statistically significant better performance than the current disclosures under TILA and RESPA. The Bureau has now finalized a rule with new, integrated disclosures (TILA-RESPA rule).
- The TILA-RESPA rule also provides a detailed explanation of how the forms should be filled out and used.
- The first new form (the Loan Estimate) is designed to provide disclosures that will be helpful to consumers in understanding the key features, costs, and risks of the mortgage loan for which they are applying. The Loan Estimate must be provided to consumers no later than three business days after they submit a loan application.
- The second form (the Closing Disclosure) is designed to provide disclosures that will be helpful to consumers in understanding all of the costs of the transaction. The Closing Disclosure must be provided to consumers three business days before they close on the loan.
- The forms use clear language and design to make it easier for consumers to locate key information, such as interest rate, monthly payments, and costs to close the loan. The forms also provide more information to help consumers decide whether they can afford the loan and to compare the cost of different loan offers, including the cost of the loans over time.
- We will examine these disclosures as well as when they need to be used in further detail.

Consumer Financial Protection Bureau (CFPB) New Integrated Disclosures

Note: These new integrated disclosures became effective October 3, 2015

- Combines several forms into two
 - Loan Estimate and Closing Disclosure
- Simplifies and improves disclosure forms for mortgage transactions
- Easier for lenders and consumers to understand
- Benefits to be gained by these new forms
 - Reduced paperwork
 - Reduced consumer confusion
 - Use of clearer language
 - Better design
 - Aids consumers in understanding complicated transactions
 - Important items highlighted
 - Interest rate, monthly payments, closing costs
 - Makes it easier to compare loans and make informed choices
 - Increased information on
 - Taxes and insurance
 - How interest rate and payment may change in the future
 - Easier for consumer to decide if the loan is right for them
 - Now, and in the future, consumer warned about keeping away from certain features
 - Example: Pre-payment penalties
 - Required service estimates more reliable for appraisal and pest inspections
 - Final loan terms and costs disclosed to customer at least 3 days prior to closing
 - Allows for consumer to compare initial and final costs
 - Improved monitoring of compliance by loan originators
 - New forms retained electronically
- Mortgages covered by the new disclosure rules are similar but there are some changes:
 - Mortgages covered:
 - Closed end consumer credit transactions secured by real estate and subject to RESPA
 - Now includes
 - Loans secured by vacant land on which a home will be constructed
 - Must use loan proceeds within two years after settlement
 - Construction-only loans
 - Not covered:
 - Home Equity Lines of Credit (HELOC)
 - Reverse Mortgages
 - Mortgages secured by a dwelling not attached to land
 - Example: Mobile home
 - Loans by creditor with five or fewer mortgages made in one year

In the following sections, “CFR” stands for “Code of Federal Regulations” and “USC” stands for “United States Code”. Once Congress passes a law it is recorded in the United States Code (USC) books, but it usually will not explain what procedures should be followed. The Code of Federal Regulations (CFR) explains how the laws are to be implemented.

The Loan Estimate

- Definition of application includes: (Regulation Z, 12 CFR §1026.2(a)(3)(i))
 - Consumer's name
 - Income
 - Social Security number to obtain a credit report
 - Property address
 - Estimate value of the property
 - Amount of mortgage loan applying for
 - Other information deemed necessary for properly underwriting and assessing the borrower's ability to repay may be requested and obtained by the mortgage loan originator
- This proposal by the CFPB will replace the "Good Faith Estimate" and the "early Truth in Lending" with the "Loan Estimate" form
 - This also includes forms specifically for more complicated products
- Loan Estimate Form - This information will be detailed more in the next section
 - First page
 - Information on borrower and loan
 - Loan terms, amount, payments and rate
 - Prepayment penalties and balloon features
 - Projected payments
 - Estimated costs to close and settlement fees
 - Second page
 - Settlement costs and fees
 - Details on escrows and down payment
 - Third page
 - Discloses payments over 5 years, Annual Percentage Rate (APR), Total Interest Payment (TIP) and several other disclosures

Delivery of the Loan Estimate

- The Loan Estimate must be delivered or placed in the mail no later than the third business day after receiving the application. (Regulation Z, 12 CFR §1026.19(e)(1)(iii))
- Business Day will now include any day the creditor's offices are open to the public to carry on substantially all of its business functions (Regulation Z, 12 CFR §1026.2(a)(6) (effective October 3, 2015))
- If the Loan Estimate is not provided to the consumer in person
 - It will be considered they received the Loan Estimate within the three business day time schedule after delivery or placed in the mail (Regulation Z, 12 CFR §1026.19(e)(1)(iv))
- If the loan application will not or cannot be approved within the three business day time period or if the application is withdrawn
 - Creditor does not have to provide a Loan Estimate (Comment 19(e)(1)(iii)-3)
- If the borrower amends the application in a favorable manner and the application process can continue
 - Creditor must comply with delivery of the Loan Estimate guidelines
 - Within three business day of receiving the updated application (Comment 19(e)(1)(iii)-3)
- The Loan Estimate must be delivered or placed in the mail not later than the seventh business day before consummation of the mortgage loan (Regulation Z, 12 CFR §1026.19(e)(1)(iii)(B))
- Borrower may waive the seven business day waiting period for a bona-fide personal financial emergency (Regulation Z, 12 CFR §1026.19(e)(1)(v)).
 - Example: Imminent sale of consumer's home at foreclosure
 - Borrower must provide lender with a
 - A dated, written statement describing the emergency
 - Explain reason for a waiver of the waiting period
 - Must be signed by all borrowers
 - Pre-printed waiver forms are not acceptable (Regulation Z, 12 CFR §1026.19(e)(1)(v))

- The Loan Estimate is still an estimate in "Good Faith"
 - Mortgage loan originators must act in good faith when assessing costs for the Loan Estimate
 - If exact dollar amount is not available when the Loan Estimate is prepared
 - Estimates may be used
 - Keep in mind, new disclosures may be required (Regulation Z, 12 CFR §1026.17(c) or 1026.19)
 - Estimated items must be shown as an "Estimate" (Comment 17(c)(2)(i)-2)
 - Good faith by lender will be determined when comparing the original Loan Estimate with the actual charges shown on the Closing Disclosure Regulation Z, 12 CFR §1026.19(e)(3)(i) and (ii)
 - If charge is in excess of original disclosed amount, this is considered not in good faith
 - If charge is less, this is considered to be in good faith
- Circumstances where mortgage loan originators can charge more than amount on Loan Estimate
 - Charged amount is within tolerance thresholds (Regulation Z, 12 CFR §1026.19(e)(3)(ii))
 - A changed circumstance allows for a revised Loan Estimate or Closing Disclosure (Regulation Z, 12 CFR §1026.19(e)(3)(iv))
- Items not subject to tolerance limitation
 - Prepaid interest (Regulation Z, 12 CFR §1026.19(e)(3)(iii)(A)-(C))
 - Charges paid to third party service provider (Regulation Z, 12 CFR §1026.19(e)(3)(iii)(E))
 - These are charges or services not required by the lender
 - Use best information available when quoting these charges (Regulation Z, 12 CFR §1026.19(e)(3)(iii))
- For items paid at closing that exceed original amount on the Loan Estimate
 - If beyond allowable threshold
 - Lender must refund excess dollar amount to the borrower
 - No later than 60 days after consummation (Regulation Z, 12 CFR §1026.19(f)(2)(v))
 - Zero tolerance items
 - Any amount charged beyond the amount disclosed on the Loan Estimate must be refunded to the consumer. (Regulation Z, 12 CFR §1026.19(e)(3)(i))
 - 10% cumulative tolerance items
 - Difference refunded to the borrower (Regulation Z, 12 CFR §1026.19(e)(3)(ii))

The Loan Estimate Document Regulation Z, 12 CFR §1026.37 (all)

The Loan Estimate sample is from the Consumer Financial Protection Bureau and is an example of a fixed rate mortgage. See sample at http://files.consumerfinance.gov/f/201403_cfpb_loan-estimate_fixed-rate-loan-sample-H24B.pdf

- **Page One**
 - **Title of the form** - "Loan Estimate"
 - The wording will include: "Save this Loan Estimate to compare with your Closing Disclosure"
 - **Date issued**
 - Date mailed or delivered to the consumer
 - **Applicants**
 - Include name and address of each applicant
 - **Property**
 - Address of property with zip code
 - If unavailable, use a description, example - lot number with a zip code
 - **Sales price**
 - For a purchase money transaction, use contract sales price
 - If no seller, use appraised value or an estimate of value
 - **Loan term**
 - Use years or months or both if applicable
 - **Purpose**
 - Purchase, refinance, construction, home equity

- **Product**
 - ARM, step rate, fixed rate
 - If any features on the loan product will change, this must be included in product description, including:
 - Negative amortization, interest only, step payment, balloon payment, or seasonal payment
 - Duration of this payment feature must be disclosed
 - Example: If the first year of payments cover interest only and will not be applied towards the principal, this type loan description would be disclosed as a One-Year Interest Only
- **Loan type**
 - Conventional, FHA, VA, etc.
- **Lender's loan identification number**
 - Identifies the transaction
- **Rate lock**
 - If yes, disclose date, time and time zone when the lock periods ends
 - Also, the date, time and time zone when the estimated closing costs will expire
- **Loan Terms Section**
 - Loan amount - Use whole dollars
 - Initial interest rate
 - Initial monthly principal and interest
 - Information on the prepayment penalty
 - Answer "Yes" or "No" in this column
 - If prepayment penalty applies,
 - Include maximum amount of penalty
 - Date the penalty ends
 - If the loan has a balloon payment
 - Answer "Yes" or "No" in this column
 - If yes, supply information on
 - Maximum amount of balloon payment
 - Due date of balloon payment
- **Can this amount increase after closing?**
 - If yes, include applicable information in regards to adjustments in the
 - Loan amount
 - Interest rate
 - Monthly principal and interest
 - If no adjustments, disclose "No"
- **Projected Payments** will show estimates of payments made during the life of the loan. Must include:
 - Principal and interest, mortgage insurance, estimated escrows, and estimates of the total monthly payment
 - Also must include an estimate of taxes, insurance, and assessments regardless if they are paid through an escrow account
 - Use a periodic table, the sample Loan Estimate demonstrates the payments in years 1-5, 6-8, 9-11, and 12-30
 - Should disclose if, and how payments will change during these different phases
 - Range of payments are for principal and interest only. Mortgage insurance and escrows are not included
- **Estimated Total Monthly Payment**
 - Each column will show the amount of principal and interest, mortgage insurance, and estimated escrow
- **Estimated Taxes, Insurance, & Assessments**
 - Must disclose, even if an escrow account will not apply
 - "Amount can increase over time" statement will be included in this section
- **Costs at Closing**
 - **Estimated Closing Costs** are detailed on page 2 of the Loan Estimate
 - **Estimated Cash to Close** will also be computed on page 2 of the Loan Estimate

- **Page 2 - Closing Cost Details**

- **Loan Costs**

- **(A) Origination Charges**

- Lists items the consumer will pay to each creditor and loan originator
 - Example: Points, application fee, underwriting fee

- **(B) Services You Cannot Shop For**

- May include: Appraisal fee, credit report fee, flood determination fee, tax monitoring fee, lender's attorney fee, upfront mortgage insurance fee

- **(C) Services You Can Shop For**

- These are services the consumer can shop for and will pay for at settlement
 - Examples: Pest inspection fee, survey fee, title insurance binder, lender's title policy, title search, examination of title
 - Cannot disclose more than 14 Services You Can Shop For. If more, disclose the total amount that exceed 13 with the label "Additional Charges". If needed, an addendum can be added to the Loan Estimate

- **(D) Total Loan Costs (A+B+C)**

- Total of these columns

- **Other Costs**

- **(E) Taxes and Other Government Fees**

- This section will include recording fees and other taxes and transfer taxes

- **(F) Prepays**

- These are items paid by the consumer in advance of the first scheduled payment
 - Include homeowner's insurance premiums, mortgage insurance premiums, prepaid interest, property taxes
 - A maximum of three additional items can be added

- **(G) Initial Escrow Payment at Closing**

- Items the consumer will place in a reserve or escrow account for homeowner's insurance, mortgage insurance, property taxes
 - Show the amount escrowed per month for each item, number of months collected, and total amount paid

- **(H) Other**

- Items the borrower is likely to pay or has contracted with a person to pay
 - Such as, owner's title insurance, credit life insurance, home owner's warranty

- **(I) Total Other Costs**

- Total of columns E, F, G and H

- **(J) Total Closing Costs**

- The sum of Total Loan Costs (D), Total Other Costs (I) and Lender Credits

- **Calculating Cash to Close**

- This section will disclose the total amount the borrower needs to close. Consists of
 - Total Closing Costs - From Section J
 - Closing costs financed
 - Borrower down payment
 - Deposit - If this is a purchase transaction
 - Funds for Borrower
 - Seller Credits - these are items paid for by the seller
 - Adjustments and Other Credits

- **Estimated Cash to Close**

- Sum of the above seven items

- **Page 3 - Additional Information About This Loan**

- First section will be contact information

- Name, NMLS ID, License ID for the creditor and the mortgage broker
 - And name, email, phone number of the individual loan originator

- Individual loan originator will be the primary contact for the borrower

- **Comparisons**
 - Must include the statement, "Use these measures to compare this loan with other loans."
 - This sections discloses
 - Loan costs on this loan in five years
 - Total principal, interest, mortgage insurance, and loan costs
 - Principal you will have paid off
 - The Annual Percentage Rate (APR)
 - Total Interest Percentage (TIP)
 - Total interest paid over the life of the loan shown as a percentage of the loan amount
- **Other Considerations**
 - Lists details about the
 - Appraisal
 - Assumption
 - Homeowner's Insurance
 - Late Payment
 - Refinance
 - Servicing
- **Confirm Receipt**
 - Borrower is not required to sign the Loan Estimate
 - Lender will have two options:
 - If a line is included for the borrower's signature, the following must be disclosed
 - "By signing, you are only confirming that you have received this form. You do not have to accept this loan because you have signed or received this form."
 - If no line is included, the following must be disclosed
 - "You do not have to accept this loan because you have received this form or signed a loan application."

The Closing Disclosure

- Has replaced these two forms
 - Final Truth in Lending form
 - HUD-1 Uniform Settlement Statement
- Provides the consumer with a detailed analysis of their mortgage transaction
- Provided three days before the closing takes place Regulation Z, 12 CFR §1026.19(f)(1)(ii)
 - This gives the consumer additional time to review their final loan documents
- Business day defined for the Closing Disclosure
 - Different from the Loan Estimate
- All calendar days except Sundays and legal holidays (Regulation Z, 12 CFR §1026.2(a)(6), 1026.19(f)(1)(ii)(A) and (f)(1)(iii))
 - Legal public holidays
 - New Year's Day
 - Martin Luther King, Jr., Birthday
 - Washington's Birthday
 - Memorial Day
 - Independence Day
 - Labor Day
 - Columbus Day
 - Veterans Day
 - Thanksgiving Day
 - Christmas Day
- The Closing Disclosure must contain the actual terms and costs associated with the loan transaction (Regulation Z, 12 CFR §1026.19(f)(1)(i)).
 - As with the Loan Estimate, lenders must act in good faith when preparing the Closing Disclosure
 - The Closing Disclosure will contain all actual terms and costs of the loan transaction (1 Regulation Z, 12 CFR §1026.19(f)(1)(i))

- Any changes in costs or terms will require a corrected disclosure delivered to the borrower
 - A new three day waiting period may be required for a corrected Closing Disclosure (1 Regulation Z, 12 CFR §1026.19(f)(2))
- Three categories of changes requiring a corrected Closing Disclosure (Regulation Z, 12 CFR §1026.19(f)(2))
 - Changes occurring
 - Before consummation not requiring a new three business day waiting period (Regulation Z, 12 CFR §1026.19(f)(2)(i))
 - Before consummation that require a new three business day waiting period (Regulation Z, 12 CFR §1026.19(f)(2)(ii))
 - After consummation (Regulation Z, 12 CFR §1026.19(f)(2)(iii))
- If any of the following changes take place after delivery of the Closing Disclosure and before consummation, a corrected disclosure will be provided to the consumer showing the changed items (Regulation Z, 12 CFR §1026.19(f)(2)(ii))
 - No later than three business days before consummation
 - Those changes are
 - APR becomes inaccurate
 - Closing Disclosure must show correct APR and any other changed terms
 - Loan product changes
 - Closing disclosure must show correct loan product and any other changed items
 - Prepayment penalty has been added
 - Closing disclosure must show the prepayment provision and any other changed items
- If terms or costs change after consummation and within a 30 day period and Closing Disclosure becomes inaccurate, a corrected Closing Disclosure must be delivered to the borrower
 - Delivery of the corrected Closing Disclosure must take place within 30 days of lender's knowledge of the error (Regulation Z, 12 CFR §1026.19(f)(2)(iii))
- Allowable fees prior to consumer's receipt of the Loan Estimate
 - Lender may not impose any fee until the Loan Estimate is received by the consumer, including: (Regulation Z, 12 CFR §1026.19(e)(2)(i)(B))
 - Application fee
 - Appraisal fees
 - Underwriting fees
 - Other fees imposed on the consumer
 - With the exception of a bona fide and reasonable fee for obtaining a consumer's credit report

The Closing Disclosure Document Regulation Z, 12 CFR §1026.38 (all)

- The Loan Estimate sample is from the Consumer Financial Protection Bureau and is an example of a fixed rate mortgage
- See sample at http://files.consumerfinance.gov/f/201311_cfpb_kbyo_closing-disclosure.pdf

Page One

- **Title of the form** - "Closing Disclosure"
 - The wording will include: "This form is a statement of final loan terms and closing costs. Compare this document with your Loan Estimate."
- Closing Information will include the following:
 - **Date issued**
 - This is the date the Closing Disclosure is delivered to the borrower
- **Closing Date** - Date of Consummation
- **Disbursement Date** - Anticipated date of disbursement of funds
- **Settlement Agent** - name of closing agent
- **File #** - closing agent's file number
- **Property** - Address or location of property, includes zip code
- **Sales Price**
 - If purchase - Contract sales price
 - If no seller - Appraised value

- **Transaction Information**
 - **Borrower** - name, mailing address
 - **Seller** - if applicable - name, mailing address
 - **Lender** - Name of lender
- **Loan Information**
 - **Loan term**
 - Use years or months or both if applicable
 - **Purpose**
 - Purchase, refinance, construction, home equity
 - **Product**
 - ARM, step rate, fixed rate
 - If any features on the loan product will change, this must be included in product description, including:
 - Negative amortization, interest only, step payment, balloon payment, or seasonal payment
 - Duration of this payment feature must be disclosed
 - Example: If the first year of payments cover interest only and will not be applied towards the principal, this type loan description would be disclosed as a One-Year Interest Only
 - **Loan type**
 - Conventional, FHA, VA, etc.
 - **Loan ID number**
 - Identifies the transaction
 - Note: The Loan Term, Purpose, Product Loan Type and Loan ID number should be updated, if needed, to reflect information regarding the transaction at consummation
- **MIC#**
 - Mortgage Insurance Case Number
- **Loan Terms Section**
 - **Loan amount** - Use whole dollars
 - **Interest rate** - rate for this loan
 - **Monthly Principal and Interest**
 - **Prepayment Penalty** - Information on the prepayment penalty, if it applies
 - If prepayment penalty applies,
 - Include maximum amount of penalty
 - Date the penalty ends
 - **Balloon Payment** - If the loan has a balloon payment
 - Maximum amount of balloon payment
 - Due date of balloon payment
- **Can this amount increase after closing?**
 - If yes, include applicable information in regards to adjustments in the
 - Loan amount
 - Interest rate
 - Monthly principal and interest
 - Prepayment Penalty
 - Balloon Payment
 - If no adjustments, disclose "No"
- **Projected Payments** will show estimates of payments made during the life of the loan. Must include:
 - Principal and interest, mortgage insurance, estimated escrows, and estimates of the total monthly payment
 - Also must include an estimate of taxes, insurance, and assessments regardless if they are paid through an escrow account
 - Use a periodic table, the sample Closing Disclosure demonstrates the payments in years 1-7 and 8-30
 - Should disclose if, and how, payments will change during these different phases
 - Range of payments are for principal and interest only
 - Mortgage insurance and escrows are not included
- **Estimated Total Monthly Payment**
 - Each column will show the amount of principal and interest, mortgage insurance, and estimated escrow

- **Estimated Taxes, Insurance, & Assessments**
 - Must disclose, even if an escrow account will not apply
 - "Amount can increase over time" statement will be included in this section
- **Costs at Closing**
 - **Estimated Closing Costs** are detailed on page 2 of the Loan Estimate
 - Other Costs Section
 - Under Total Closing Costs
 - This section includes amounts from
 - Total Loan Costs - Section D
 - Total Other Costs - Section I
 - Lender Credits - Section J
- **Cash to Close**
 - Estimated cash the borrower will pay or receive at the closing
 - Same as page three of the Closing Disclosure
 - Under heading Cash to Close in the Calculating Cash to Close section, top of page three

Page Two Closing Costs Details

- **Loan Costs**
 - Note - Items in the Loan Costs and Other Costs sections can be expanded and deleted for space control - Although, if an item is required to be disclosed it may not be deleted, even though it is not applicable. As an example, "Points" located in the Origination Section must remain regardless if there is a charge or this item.
 - Loan Costs and Other Costs are allowed to be disclosed on separate pages of the Closing Disclosure. The pages will be numbered Page 2a and 2b.
 - There are items in the Loan Costs section that will be somewhat the same as disclosed on the Loan Estimate. You can update some items to reflect the terms and details of the loan at consummation, unless specified below.
 - This page will consist of five columns for
 - Borrower-Paid
 - At Closing
 - Before Closing
 - Seller- Paid
 - At Closing
 - Before Closing
 - Paid by Others
- **(A) Origination Charges**
 - Charges for making this loan
 - Points are shown in dollar amount and percentage of the loan amount
 - Itemization and a subtotal of each amount paid to each creditor and loan originator
- **(B) Services Borrower Did Not Shop For**
 - Shows dollar amount and a list of items the borrower did not shop for
 - Appraisal Fee,
 - Credit Report Fee,
 - Flood Determination Fee,
 - Flood Monitoring Fee,
 - Tax Monitoring Fee,
 - Tax Status Research Fee
- **(C) Services Borrower Did Shop For**
 - Shows dollar amount and a list of items the borrower shopped for
 - Pet inspection fee,
 - Survey Fee,
 - Title Insurance Binder,
 - Lender's Title Insurance,
 - Settlement Agent's Fee,
 - Title Search
- **(D) Total Loan Costs**
 - Total of A, B, and C of the Borrower-Paid section

- Other Costs
 - **(E) Taxes and Other Government Fees**
 - Paid to state and local government agencies
 - Transfer Taxes section will itemize the amount paid by the borrower and the seller
 - **(F) Prepays**
 - These are items paid by the consumer in advance of the first scheduled payment
 - Include homeowner's insurance premiums, mortgage insurance premiums, prepaid interest, property taxes
 - A maximum of three additional items can be added
 - **(G) Initial Escrow Payment at Closing**
 - Items the consumer will place in a reserve or escrow account for homeowner's insurance, mortgage insurance, property taxes
 - Show the amount escrowed per month for each item, number of months collected, and total amount paid
 - **(H) Other**
 - Includes costs incurred by the borrower or seller, but were not required to be part of the Loan Estimate
 - Home Inspection Fee,
 - Home Owner's Warranty Fee
 - **(I) Total Other Costs**
 - Total of columns E, F, G and H
 - **(J) Total Closing Costs**
 - Borrower-Paid - All closing costs added with the Lender Credit amount subtracted from this total
 - Lender Credits are disclosed as Borrower-Paid At Closing

Page Three - Calculating Cash to Close

Includes this notice, "Use this table to see what has changed from your Loan Estimate."

- Three columns
 - Amount disclosed on Loan Estimate
 - Final amount
 - And a "Did this change?" section
 - If yes, give a description of where the changed amounts can be found within the Closing Disclosure
- This section includes information regarding
 - Total Closing Costs
 - Same as page two of Closing Disclosure
 - If increase exceeds the legal limits, show in "Did this change?" column
 - Closing Costs Paid Before Closing
 - Down Payment/Funds from Borrower
 - Deposit
 - Funds for Borrower
 - Seller Credits
 - Adjustments and Other Credits

Summaries of Transactions - Includes the notice, "Use this table to see a summary of your transaction."

- Used for purchase transactions
- **K. Due from Borrower at Closing**
 - Sales price of property, sales price of any personal property, closing costs paid by seller, adjustments and adjustment for items paid in advance by the seller
- **L. Paid Already by or on Behalf of Borrower at Closing**
 - Deposit - paid into a trust account by the borrower
 - Loan amount
 - Existing Loan(s) Assumed or Taken Subject to
 - List any loans the borrower is assuming in this transaction
 - Seller Credit
 - Credit to the borrower from the seller

- Other Credits
 - From other entity other than the borrower or the seller
- Adjustments for Items Unpaid by Seller
 - Due to borrower if paid in arrears
 - Example: taxes on the property are paid on an annual basis
- **Calculation**
 - Total Due from Borrower at Closing
 - Amount taken from Section K
 - Total Paid Already by or on Behalf of Borrower at Closing
 - Amount taken from Section L
 - Cash to Close
 - If borrower owes money check the "From" box
 - If borrower is receiving money check the "To" box
- **Seller's Transaction**
- **M. Due to Seller at Closing**
 - Will include sales price of the property being purchase and any other personal property included in the sale
 - Adjustments for Items Paid by Seller in Advance
 - Includes any adjustment for property taxes, assessments, Home Owner Association Dues that will be credited to the seller
- **N. Due from Seller at Closing**
 - Items seller will pay for at the closing include
 - Excess Deposit
 - Closing Costs Paid at Closing from Section J of the Closing Disclosure
 - Existing Loan(s) Assumed or Taken Subject to
 - Payoff of First Mortgage Loan
 - Payoff of Second Mortgage Loan
 - Seller Credit
 - Adjustments for Items Unpaid by Seller
 - Includes taxes and assessments
- **Calculation**
 - Total Due from Seller at Closing
 - Amount taken from Section M
 - Total Paid Already by or on Behalf of Seller at Closing
 - Amount taken from Section N
 - Cash to Close
 - If seller owes money check the "From" box
 - If seller is receiving money check the "To" box

Page 4 Additional Information About This Loan - Loan Disclosures

- **Assumption**
 - If the borrower sells or transfer the property, can another person assume the original terms of this loan?
- **Demand Feature**
 - Is there a demand feature that can require an early repayment of this loan?
- **Late Payment**
 - Terms of the late payment feature will include amount of time that passes before a fee will be assessed and how fee is calculated
- **Negative Amortization (increase in Loan Amount)**
 - Will regular payments pay all of the interest due for each month?
- **Partial Payments**
 - Will the lender accept partial payments? If so, in what increments?
- **Security Interest**
 - Description of the property

- **Escrow Account**
 - Lets borrower know whether or not this loan includes escrow payments
 - If included, chart will show
 - Amount of escrow property costs over the first year, listing costs paid by the account
 - Amount of non-escrow property costs over the first year, listing costs that will not be paid by the escrow account
 - Initial escrow payment
 - Monthly escrow payment
- Two notices included on this page:
 - "You may lose this property if you do not make your payments or satisfy other obligations for this loan."
 - "In the future, your property costs may change and, as a result, your escrow payment may change. You may be able to cancel your escrow account, but if you do, you must pay your property costs directly. If you fail to pay your property taxes, your state or local government may (1) impose fines and penalties or (2) place a tax lien on this property. If you fail to pay any of your property costs, your lender may (1) add the amounts to your loan balance, (2) add an escrow account to your loan, or (3) require you to pay for property insurance that the lender buys on your behalf, which likely would cost more and provide fewer benefits than what you could buy on your own."

Page 5

- **Loan Calculations**
 - **Total Payments** - this is the sum of all the borrower will have paid after all payments of principal, interest, mortgage insurance, and loan costs have been paid
 - **Finance Charge** - shows what the loan amount will cost in finance charges
 - **Amount Financed** - Loan amount available once the upfront finance charge has been paid
 - **Annual Percentage Rate** - What the costs for this loan will cost expressed as a rate
 - This is not to be confused with the actual interest rate
 - **Total Interest Percentage (TIP)** - Total amount of interest paid over the life of the loan as a percentage of the loan amount
- **Other Disclosures**
 - **Appraisal**
 - Discusses the borrower's rights in relation to the appraisal
 - **Contract Details**
 - Informs the borrower the note and security instrument have information regarding
 - What will happen if the borrower fails to make payments
 - What is default
 - Situations where the lender can require early repayment of the loan
 - Rules for making payments before they are due
 - **Liability After Foreclosure**
 - Statement letting borrower know if State law protects them from liability for any unpaid balance
 - **Refinance**
 - Information regarding the borrower's ability to refinance this loan
 - **Tax Deductions**
 - Information about deductions for interest
 - If you borrow more than the property's worth, interest on the loan amount above the property's fair market value will not be deductible
 - **Questions**
 - Website information on the CFPB
 - If the borrower has questions, wants to make a complaint, or contact the Consumer Financial Protection Bureau
 - **Contact Information**
 - Provides contact information on the
 - Lender, Mortgage Broker, Real Estate Broker for the Buyer, Real Estate Broker for the Seller, and Settlement Agent
 - Information includes
 - Name, address, NMLS ID, ST License ID, contact name, contact's NMLS ID and ST License ID, email, and phone

- **Confirm Receipt**
 - Borrower is not required to sign the Closing Disclosure
 - Lender will have two options:
 - If a line is included for the borrower's signature, the following must be disclosed
 - "By signing, you are only confirming that you have received this form. You do not have to accept this loan because you have signed or received this form."
 - If no line is included, the following must be disclosed
 - "You do not have to accept this loan because you have received this form or signed a loan application."