I. Real Estate Principles of Finance

A. Mortgage Law
   1. A mortgage is a voluntary lien on real estate, given by the mortgagor to secure the payment of a debt or the performance of an obligation to the mortgagee
      a. Mortgagor = borrower; mortgagee = lender
      b. Title theory states - the mortgagor give the mortgagee legal title and retains equitable title. Legal title is returned to the mortgagor upon full payment of the debt
      c. Lien theory states - the mortgagor retains legal and equitable title. The mortgagee has only a lien on the property as security for the debt. The lender must initiate foreclosure proceedings to obtain legal title
      d. Intermediate theory states - based on title theory, but requires the lender to foreclose to obtain legal title. Distinctions must be made under the specific state’s laws

B. Security and Debt
   1. Any interest in real estate that may be sold may also be used as security (collateral) for a debt
   2. Mortgage loan instruments
      a. Two documents must be signed
         1). The promissory note (financing instrument), the written promise to repay the debt
         2). The mortgage (security document), the document that creates the lien or transfers an interest to the creditor
      b. Hypothecation - pledging property as collateral without giving up its possession
      c. Deed of trust
         1). Similar to, but not identical to, a mortgage
         2). Creates a three-party agreement
         3). Conveys “naked title” or “bare legal title” to the third party (the trustee) who has certain obligations to the lender (the beneficiary); the borrower is the trustor
         4). Generally provides simpler and faster foreclosure than a mortgage
         5). Can be used to secure multiple promissory notes

C. Provisions of the Note
   1. The promissory note
      a. Will contain the amount of the debt, the time and method of payment, and the rate of interest
      b. If used with a mortgage, will be payable to the lender
      c. If used with a deed of trust, can be payable “to bearer”
      d. Can refer to or repeat several of the clauses contained in the mortgage or the deed of trust
      e. Is a negotiable instrument, holder of note - payee; may transfer right of the future payments
         1). By signing the instrument over to third party
         2). By delivering the instrument to the third party
   2. Interest
      a. A charge for the use of money
      b. May be due at the end of each payment period - interest in arrears (the normal method of interest payment)
      c. May be due at the beginning of each payment period - interest in advance
   3. Usury
      a. Charging interest in excess of maximum rate that may be legally charged
      b. Maximum rate generally set by state law, except when federally-preempted
      c. Some states set fixed amount, others have floating interest rate
   4. Prepayment
      a. Borrower may pay off loan in full at any time before the end of the term of the loan, or make additional payments to principal during the term
      b. Penalties may be assessed by the lender to compensate for unearned interest when a loan is paid in full prior to the scheduled end of the loan term
         1). Prepayment penalties may be regulated by state law
         2). Prepayment penalties prohibited on mortgage loans insured or guaranteed by federal government
D. Provisions of the Mortgage Document or Deed of Trust
   1. Refers to the terms of the note and clearly established that the property is security for the debt
   2. Duties of the mortgagor or trustor
      a. Payment of the debt in accordance with the terms of the note
      b. Payment of real estate taxes
      c. Maintenance of adequate insurance to protect the lender’s interest in the property
      d. Maintenance of the property to keep it in good repair
   3. Provisions for default
      a. The lender may accelerate the maturity of the debt - acceleration clause
      b. The lender can step in to pay the real estate taxes or insurance, or physically repair or maintain the property
   4. Assignment of the mortgage
      a. The note can be sold to a third-party investor
      b. The securing mortgage or deed of trust will be assigned with the note to its purchaser
      c. When debt is paid in full (satisfied) assignee is required to execute the satisfaction (release) of the security instrument
   5. Release of the mortgage lien
      a. The defeasance clause requires the execution of a satisfaction of mortgage (release of mortgage or mortgage discharge)
      b. The deed of trust requires the execution of a release deed or deed or reconveyance
   6. Tax and insurance reserves
      a. Required for some mortgages by the lender; called reserve fund, impound or trust or escrow account
      b. Accounts set up for real estate taxes and insurance premium
      c. RESPA limits the amount that can be held as reserves
   7. Buying subject to or assuming a seller’s mortgage or deed of trust
      a. Subject to:
         1). The purchaser is not personally liable for the debt
         2). In the event of a foreclosure, the purchaser is not personally liable for a deficiency
      b. Assumption
         1). The purchaser is personally liable for the debt
         2). In the event of a foreclosure, the purchaser may be held liable for any deficiency
         3). Unless specifically released by the lender, the original borrower may also be liable for the debt or any deficiency
         4). Loan may not be assumed in many cases without lender approval, requiring asserter to qualify
   8. Alienation clause
      a. Also called a resale clause, due-on-sale clause, or call clause
      b. The lender can declare the entire debt due immediately
      c. The lender can raise the interest rate to the market rate
   9. Recording mortgages and deeds of trust
      a. Recorded in the county where the property is located
      b. Gives constructive notice of the debt
      c. Establishes lien’s priority

E. Provisions of Land Contracts (Installment Contract or Contract for Deed)
   1. The buyer (the vendee) agrees to make a down payment and periodic payments of principal and interest and receives equitable title at the signing of the contract
   2. The seller (the vendor) retains legal title during the contract term and agrees to convey legal title to the buyer when the terms of the contract have been fulfilled
   3. Contract permits eviction in case of default with the seller keeping any money already paid

F. Foreclosure - the legal procedure whereby the property pledged as collateral is sold to satisfy the debt
   1. Methods of foreclosure - provisions vary from state to state
      a. Judicial foreclosure - the property may be sold by court order
      b. Non-judicial foreclosure - used when a power-of-sale clause is contained in the security document
      c. Strict foreclosure - after proper notice is given and the defaulted debt remains unpaid, the court awards legal title to the lender
      d. All junior liens are eliminated
   2. Deed in lieu of foreclosure
      a. Sometimes called a “friendly foreclosure” (“dation en paiement” in Louisiana)
      b. The borrower forfeits any equity in the property and deeds it to the lender
c. Any junior liens remain and become the lender's liability

d. Lender loses any rights pertaining to FHA or PMI insurance and/or VA guarantees

3. Redemption
   a. Provides the opportunity for a defaulting borrower to redeem the property
   b. Equitable right of redemption - any time before the foreclosure sale, the defaulted borrower can bring the debt current and have it reinstated
   c. Statutory right of redemption - the specific period allowed for redemption after the foreclosure sale; state laws vary widely

4. Deed to purchaser at sale
   a. Given after any redemption period has expired
   b. Executed by a sheriff or a master-in-chancery
   c. Contains no warranties

5. Deficiency judgment
   a. Issued to cover the difference between the amount received at the foreclosure sale and the principal balance owed
   b. Becomes a judgment against the debtor

II. Real Estate Practices of Finance
   A. Introduction to the Real Estate Financing Market
      1. Federal Reserve System
         a. Created to help maintain sound credit conditions
         b. Helps counteract inflationary and deflationary trends
         c. Attempts to create a favorable economic climate
         d. Country is divided into twelve federal reserve districts
         e. Regulates the flow of money and interest rates
            1). Controls bank reserve requirements
               a). Funds available for loans or any other use
               b). Designed primarily to protect customer deposits
               c). Also provides a means of manipulating the flow of cash into the money market
            2). Controls bank discount rates
               a). When banks borrow from their district reserve banks, their loan interest rate determines what interest rate they must charge their borrowers
               b). A high discount rate reduces consumer borrowing; a low discount rate stimulates consumer borrowing

   B. The Primary Mortgage Market
      1. Lenders provide funds to borrowers as investments
         a. Income generated for lender from
            1). Finance charges, loan origination fees, and discount points
            2). Recurring income-interest
         b. Selling loans in secondary mortgage market
            1). Generate funds to make new loans
            2). Servicing loans
               a). Collecting payments, accounting, bookkeeping, processing payments of taxes and insurance, and following up on delinquencies
      2. Thrifts, savings associations, and commercial banks
         a. Fiduciary lenders
         b. Subject to regulations set by government agencies such as:
            1). Federal Deposit Insurance Corporation (FDIC)
            2). Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA)
      3. Insurance companies
         a. Invest much of their premium income in profitable enterprises, such as long-term real estate loans
         b. Prefer income producing commercial and industrial properties
         c. Invest in residential loans by purchasing large blocks of government backed loans from the Federal National Mortgage Association (FNMA) and other mortgage warehousing agencies
         d. Often invest by demanding an equity position in the property
      4. Credit unions
         a. Cooperative organizations that require membership to borrow
b. Only recently started making long-term first and second loans

5. Pension funds
   a. Only recently started making long-term first and second mortgage loans
   b. Funds channeled through mortgage bankers and mortgage brokers

6. Endowment funds
   a. Commercial banks and mortgage bankers handle
   b. Source for financing low-risk commercial and industrial property

7. Investment group financing
   a. Very popular for large real estate projects
   b. Funds come from such sources as partnerships and investment trusts

8. Mortgage banking companies
   a. Originate real estate loans using funds borrowed from others as well as their own funds
   b. Often serve as intermediaries between investors and borrowers, but not as mortgage brokers
   c. Generally service the loan once it has been made
   d. Usually organized as stock corporations
   e. Usually subject to fewer restrictions than other lenders

9. Mortgage brokers
   a. Act as intermediaries between borrowers and lenders
   b. Locate borrowers, process their loan applications and submit them to lenders
   c. Do not service the loan once it has been made

C. The Secondary Mortgage Market
   1. Secondary mortgage market - where loans are bought and sold after they have been funded
   2. The originating lender usually services the loan for a fee
   3. Warehousing agencies - purchase real estate loans and then assemble them into securities for sale to investors
      a. A quasi-government agency - a privately owned stock-issuing corporation backed by the federal government
      b. Deals in all real estate loans - FHA, VA, and conventional
      c. Guarantees payment of principal and interest to holders of its mortgage-backed securities
      d. Buys block or pool of mortgages from a lender in exchange for mortgagee-backed securities
   5. Government National Mortgage Association (GNMA, “Ginnie Mae”)
      a. Exists as a division of HUD
      b. Administers special assistance programs for real estate loans
      c. Works with FNMA in the secondary mortgage market
      d. Joins with FNMA to provide “tandem plan” funds in times of high interest rates and tight money
      e. Issues the GNMA pass-through certificates
         1). A security interest in a pool of mortgages
         2). It “passes through” the principal and interest payments, directly to the holder of the certificate
         3). The payments are guaranteed by GNMA
   6. Federal Home Loan Mortgage Corporation (FHLMC, “Freddie Mac”)
      1. Provides a secondary market primarily for conventional loans
      2. Sells mortgage-backed securities like FNMA
      3. Unlike GNMA, FHLMC does not guarantee any payments

D. Financing Techniques - although the term “mortgage” is used throughout this chapter, the provisions also apply to deeds of trust loans
   1. Straight loans
      a. Also called “term loans” or “non-amortizing loans”
      b. Periodic payments of interest only with the entire principal balance due at the end of the loan term
      c. Generally used for home improvement and second mortgages
   2. Amortized loans
      a. Also called “direct reduction” loans
      b. Level-payment mortgages
         1). Each payment is the same dollar amount
         2). The amount applied to the interest decreases with each payment
         3). The amount applied to the principal increases with each payment
      c. Regular periodic payments are made, with each payment being applied first to the interest owed and the balance to the principal amount
      d. End of term all principal is paid off
Most amortized loans paid in monthly installments; some paid quarterly or semi-annually

3. Adjustable rate mortgages
   a. Interest rates fluctuate, and therefore, so do the payments
   b. Components include:
      1. Interest rate tied to the movement of an index
      2. Interest rate equals the index rate plus a premium, the margin - the lender’s profit and cost of doing business
      3. Rate caps that limit the amount the rate can increase both periodically and over the life of the loan
      4. Payment cap that sets the maximum payment amount (might cause negative amortization)
      5. Adjustment period that sets how often the rate can be changed

4. Balloon payment loans
   a. The periodic payments are not sufficient to fully repay the principal loan balance by the end of the term of the loan
   b. Characteristic of a partially-amortized loan

5. Reverse annuity mortgages (RAMs)
   a. Regular monthly payments made to the borrower
   b. The accrued debt (principal and interest) becomes payable at some specified future event, such as the sale of the property or by the estate upon the death of the owner

E. Loan Programs
1. Loans are classified based on the loan-to-value ratio
   a. Value based on the sale price or appraisal, whichever is lower
   b. Lower the ratio of debt to value, the higher the down payment; a more secure loan, minimizes lender’s risk

2. Conventional loans
   a. Loan-to-value ratio lowest; borrower make significant down payment
   b. Security for the loan is provided solely by the mortgage
   c. Payment of debt rests solely on the ability of the borrower to pay based on the borrower’s:
      1. Creditworthiness as indicated by credit reports
      2. Amount of income
      3. Amount of existing outstanding debt

3. Private mortgage insurance
   a. Loan-to-value ratio higher than for other conventional loans
   b. Additional security for the loan for the lender provided by private mortgage insurance
   c. 20 to 25 percent of the loan is insured
   d. Borrower pays insurance premium to the lender
   e. PMI to drop automatically when loan-to-value is 22%

4. FHA insured loans
   a. FHA - part of the Department of Housing and Urban Development (HUD)
   b. FHA insures real estate loans made by approved lending institutions
   c. Most common program: Title II, Section 203(b)
      1. For one to four family residences
      2. Borrower or someone else pays mortgage insurance premium (MIP) in cash or it may be financed
      3. FHA sets standards for the type and construction of buildings and neighborhood and qualifications for borrowers
   d. Other FHA loan programs - for home improvement purposes, for condominium units, and adjustable rate mortgage loans
   e. Prepayment privileges - no penalty to prepay as long as the lender receives minimum thirty days notice
   f. Assumption rules - depends on when loan was originated
      1. Loans before December, 1986 - generally no restrictions
      2. Loans between December 1, 1986 and December 14, 1989 - the buyer must submit to a creditworthiness review
      3. Loans after December 15, 1989 - no assumption without complete buyer qualification
   g. Discount points - who pays them and in what amount is negotiable between the parties; concessions exceeding six percent of the sales price will trigger a reduction in the property’s appraised value

5. VA guaranteed loans
a. The Department of Veterans Affairs (VA)
   1) Authorizes the guarantee of home loans for eligible veterans
   2) Sets the minimum service times of 90 days, 181 days or two years, depending on the calendar dates of
      service
   3) Reservists who do not otherwise qualify are also eligible
b. VA guarantees real estate loans made by approved lending institutions
c. Financing provisions:
   1) Generally no down payment is required
   2) There is no limit on the amount of the loan; determined by lender
   3) Limit on the maximum amount of VA guarantee
      a). Loans up to $45,000 - 50%
      b). $45,001 to $56,250 - $22,500
      c). $56,251 to $203,000 - the lesser of $36,000 or 40% of the loan
      d). More than $203,000 - the lesser of $50,750 or 25% of the loan
   4) The veteran must apply for a certificate of eligibility that indicated the maximum guarantee to which the
      veteran is entitled
   5) The VA will issue a certificate of reasonable value (the VA approved appraisal)
      a). To indicate the property’s maximum value for guarantee purposes
      b). If property does not appraise, veteran can make a down payment to make up the difference between
         the appraisal and sale price
d. Fees
   1) Loan origination fee paid to lender
   2) Funding fee paid to VA
   3) Discount points - can be paid by the veteran, seller or other person but cannot be financed
e. Prepayment privileges - can prepay without any penalty
f. Other Financing Techniques
   1. Purchase-money mortgage
      a). Usually refers to an extension of credit by the seller to the buyer that enables the buyer to purchase the
         property
      b). The seller “takes back” a note for some or all of the purchase price
   2. Package loans
      a). One loan covering both real and personal property
      b). Usually used in new home sales to include the financing for floor and window coverings, major appliances,
         and other similar items of personal property
   3. Blanket loans
      a). One loan secured by multiple parcels of property as collateral
      b). Usually used in the financing of subdivision developments
      c). Partial release clause enables borrower to get a release of one of the parcels while the lien remains in place
         on the other parcels
   4. Open-end loans
      a). Secures a note for a current loan and for any future advances
      b). Sometimes called an “equity line of credit”
      c). Borrower can “open” the loan to increase the debt to its original amount
   5. Construction loans
      a). Periodic payments often called “progress payments” or “draws”
      b). Made to the general contractor at predetermined progress points
      c). Paid off and replaced by a permanent or “take out” loan
   6. Sales and leasebacks
      a). The seller sells the property and leases it back, receiving cash and the use of the property; becomes the
         lessee
      b). The buyer receives the income from a fully leased building
      c). Transactions usually require expert legal and tax advice
   7. Home equity loans
      a). Usually beneath the loan obtained to purchase the property
      b). Can be an equity line of credit or a fixed amount
G. Financing Legislation
   1. Truth-in-Lending Act and Regulation Z
      a). Requires lenders to disclose to borrowers the true cost of obtaining credit so that interest rates among lenders
can be compared
b. Applies to all loans of $25,000 or less for private consumers
c. Always applies when a residence collateralizes the loan
d. Does not apply to agricultural loans over $25,000, or business or commercial loans of any amount
e. The consumer must be fully informed of all financing charges, including loan origination fees, finders’ fees, service charges, discount points, and interest charges
f. The lender must compute and disclose the annual percentage rate (APR) - the true cost of the financing to be obtained
g. For purposes of Regulation Z, a creditor is defined as one who:
   1). Extends consumer credit more than 25 times a year or more than five times a year if the transaction involves a dwelling as security
   2). Subjects the credit to a finance charge or contracts for payments in more than four installments
h. Three-day right of rescission
   1). Applies to most Regulation Z consumer credit transactions
   2). Does not apply to residential purchase money or first mortgage or deed of trust loans
i. Advertising for real estate financing
   1). Must give the annual percentage rate
   2). Must specify the total finance charges
   3). If any specific loan terms are to be mentioned, all terms must be included such as the cash price, required down payment, number, amounts, and due dates of all payments, and the percentage rate
j. Penalties for noncompliance include:
   1). Liability to the consumer for twice the amount of the finance charge with a $100 minimum and a $1,000 maximum
   2). Court costs, attorney’s fees and actual damages
   3). Fines of up to $10,000 for each day a violation continues after an administrative order enforcing Regulation Z is given or for engaging in unfair or deceptive credit practices
   4). For willful violations, up to a $5,000 fine or one year in prison or both
2. Federal Equal Credit Opportunity Act (ECOA)
a. Prohibits lenders and those who grant or arrange credit to consumers from discriminating on the basis of:
   1). Race
   2). Color
   3). Religion
   4). National origin
   5). Sex
   6). Marital status
   7). Age (provided the applicant is of legal age)
   8). Dependence on public assistance (welfare)
b. Lenders and creditors must inform rejected credit applicants, in writing, within 30 days, why credit was denied or terminated

III. Real Estate Appraisal
A. Value - the monetary worth arising from the ownership of a desired object
   1. Characteristics of value (“DUST”)
      a. Demand - the need or desire for possession or ownership backed by the financial means to satisfy that need
      b. Utility - the capacity to satisfy human needs and desires
      c. Scarcity - a finite or limited supply
      d. Transferability - the relative ease with which ownership rights can be transferred
   2. Market value
      a. The most probable price a property will bring in a fair sale
         1). In a competitive and open market
         2). The buyer and seller are each acting prudently, knowledgeably and without undue influence
         3). Price not affected by unusual circumstances
      b. Essential to determine market value
         1). The most probable price is not average or highest price
         2). The buyer and seller must be unrelated and acting without undue pressure
         3). Both the buyer and the seller must be well informed of the property’s use and potential, including its
4. A reasonable length of time must be allowed for the property to be exposed in the open market
5. Consideration paid in cash or its equivalent
6. Price must represent a normal consideration, unaffected by special financing

3. Market value versus market price
   a. Market value - an estimate based on the analysis of comparable sales and other pertinent market data
   b. Market price - what the property actually sold for; sales price

4. Market value versus cost
   a. Common misconceptions that cost represents market value
   b. Cost and market value may be the same if improvements are new

5. Basic principles of value - primarily economic principles
   a. Anticipation - value can increase or decrease if one anticipates some future benefit or detriment from the property
   b. Change - no physical or economic condition remains constant
   c. Competition - excess profits tend to attract competition
   d. Conformity - maximum value is realized if the use of the land conforms to existing neighborhood standards
   e. Contribution - the value of any component of a property is what its addition contributes to the value of the whole or what its absence detracts from the value of the whole
   f. Highest and best use - the most profitable single use to which a property can be adapted. Must be:
      1). Legally permitted
      2). Financially feasible
      3). Physically possible
      4). Maximally productive
   g. Increasing and diminishing returns - improvements to land and structures will eventually reach a point at which they will no longer have a positive effect on property value
   h. Plotage - the merging or consolidation of adjacent lots held by separate owners into one larger lot may produce a higher total value than the sum of the two lots valued separately
   i. Regression and progression - between dissimilar properties, the worth of the better property is affected adversely by the presence of the lesser quality property; usually, the higher valued property decreases significantly, while the lesser valued property increases slightly
   j. Substitution - the maximum value of a property tends to be set by the cost of purchasing an equally desirable replacement

B. The Three Approaches to Value
   1. The sales comparison approach
      a. An estimate of value is obtained by comparing the subject property (the property under appraisal) with recently sold comparable properties (properties similar to the subject)
      b. The factors for which adjustments to the comparable properties are made
         1). Property rights - in cases where less than the full bundle of rights is involved
         2). Financing concessions - events such as differences in mortgage loan terms or owner financing
         3). Conditions of sale - motivational factors such as foreclosure or a sale between family members
         4). Date of sale - changes in economic conditions between the date of the sale of the comparable property and the date of the appraisal
         5). Location - compensate for locational or neighborhood differences
         6). Physical features and amenities - physical differences between the comparable properties and the subject
      c. A dollar value or percentage adjustment is assigned to each difference between the subject property and the comparable properties
      d. Adjustments are made as follows:
         1). If the comparable property is better than the subject property or has a feature that the subject property lacks, the value of the comparable is decreased accordingly
         2). If the comparable property is not as good as the subject property or lacks a feature that the subject property has, the value of the comparable is increased accordingly
   2. The cost approach
      a. Steps in the cost approach to value
         1). Estimate the value of the land as if it were vacant and available to be put to its highest and best use
         2). Estimate the current cost of constructing the building(s)
         3). Estimate the amount of accrued depreciation resulting from physical deterioration, functional obsolescence and external obsolescence
         4). Deduct the accrued depreciation from the estimated construction cost of new building(s)
5. Add the estimated land value to the depreciated cost of the building(s) and site improvements to arrive at the total property value

b. Reproduction cost versus replacement cost
   1. Reproduction cost - the current cost of a duplicate of the subject property, including both the benefits and the negative features of the property
   2. Replacement cost - the current cost of improvements with utility or function similar to the subject property

c. Determining reproduction or replacement cost new
   1. Square-foot method - based on the average cost per square foot or cost per cubic foot of recently built similar structures; also called the comparison method
   2. Unit-in-place method - replacement cost based on the installed costs of the structure’s components; also called the segregated cost or the component cost method
   3. Quantity survey method - the cost of the raw materials, plus the cost of the construction labor, plus indirect costs
   4. Index method - a factor representing the percentage of increase or decrease in construction costs to the present time is applied to the original costs of the improvements

d. Depreciation
   1. Physical deterioration - normal wear and tear
      a). Curable - repairs that are economically feasible
      b). Incurable - repairs that are not economically feasible
   2. Functional obsolescence - outmoded items and poor design
      a). Curable - outdated physical or design features that could be replaced or redesigned economically
      b). Incurable - outdated physical or design features that could not be replaced or redesigned economically or physically
   3. External obsolescence - incurable, because it is caused by a problem external to the property and, therefore, beyond the property owner’s control

e. Depreciation is usually calculated on a straight-line basis (age-life method), the assumption being that depreciation occurs at an even rate over the structure’s economic life
f. Cost approach used for appraising newer or special-use buildings, such as schools, churches, and public buildings

3. The income approach - based on the present value of the rights to future income
   a. Income divided by rate equals value (IRV)
   b. Steps in the income approach to value
      1. Estimate the annual potential gross income - income from all sources, including rent, concessions, and vending
      2. Deduct for vacancies and collection losses (“bad debt”) to obtain the effective gross income
      3. Deduct the annual operating expenses to obtain the net operating income, does not include:
         a). Debt service (principal and interest payments)
         b). Depreciation (a non-cash expense)
         c). Capital expenditures/capital improvements
         d). The owner’s personal income tax liability
      4. Estimate the price an investor would pay for the income produced by this particular type and class of property
         a). Compare the annual net operating incomes of recently sold similar properties to the sales price of those properties
         b). The annual net operating income divided by the sales price results in the capitalization (“cap”) rate
      5. Apply the capitalization rate to the subject property’s annual net operating income to obtain an estimated value

IV. Fair Housing and Ethical Practices
A. Equal Opportunity in Housing
   1. All real estate licensees must be aware of federal, state and local fair housing laws
   2. Purpose of the laws is to create an open, unbiased housing market in which every person has the opportunity to live where he or she chooses within his or her ability to pay
   3. State and local laws may be more restrictive than federal law
   4. Civil Rights Act of 1866 - prohibits discrimination in housing based on race, without exception.
B. Fair Housing Act (Title VII of the Civil Rights Act of 1968) - prohibits discrimination in housing, amended by the Housing and Community Development Act of 1974 and the Fair Housing Amendments Act 1988

1. Protected classes:
   a. Race
   b. Color
   c. Religion
   d. Sex
   e. Handicap
   f. Familial status
   g. National origin

2. Equal Housing Opportunity Poster
   a. Refusing to sell, rent, or negotiate the sale or rental of housing
   b. Making a dwelling unavailable to any person
   c. Changing terms, conditions, or services for different individuals as a means of discrimination
   d. Advertising that restricts the sale or rental of residential property
   e. Representing that a property is not available for sale or rent when, in fact, it is
   f. Profiting by inducing owners of housing to sell or rent because of the prospective entry into the neighborhood of persons in the protected classes
   g. Altering the terms or conditions of a home loan or denying a loan as a means of discrimination
   h. Denying membership or participation in any multiple listing service, real estate organization or other facility related to the sale or rental of housing as a means of discrimination

3. Definitions
   a. Housing - “dwelling” - any building or part of a building designed for occupancy by one or more families
   b. Familial status - one or more individuals who have not reached to age of 18 being domiciled with a parent, guardian, or other person with legal custody
   1) All properties available, under same terms and conditions as for others
   2) Cannot use advertising or occupancy standards with the intent or effect of restricting families with children
   c. Disability - physical or mental impairment (or having a history of same) that substantially limits one or more major life activities
   1) Does not include current illegal use of or addiction to a controlled substance
   2) Does protects individuals in addiction recovery programs
   3) Must provide accommodations and allow reasonable modifications at tenant’s own expense

C. Fair Housing Practices
1. Blockbusting - inducing homeowners to sell by marketing representations regarding the entry or prospective entry into the neighborhood by people in the protected classes
2. Steering - channeling homeseekers into or out of particular areas on the basis of race, color, religion, national origin or other protected class; the effect of limiting choices
3. Advertising - language that indicates a preference or limitation is discriminatory, such as:
   a. Cannot attract one population to exclusion of others
   b. Selection of media
4. Appraising - cannot consider factors related to the protected classes when preparing valuations or appraisals
5. Redlining - refusing to make mortgage loans or issue insurance policies in specific areas without regard to the economic qualifications of the applicant

D. Enforcement of the Fair Housing Act
1. Administered by the Office of Fair Housing and Equal Opportunity (OFHEO) under the direction of the Secretary of HUD
2. A complainant has one year after the alleged act of discrimination to file a charge with HUD, or two years to bring a federal suit
3. HUD will investigate to see if discrimination actually occurred. HUD will attempt to resolve by reconciliation
4. Unless someone connected with the charge requests that it be heard in federal district court, an administrative law judge from HUD will hear the charge
5. The administrative law judge has the authority to issue an injunction, award actual damages and impose civil penalties of:
   a. Up to $10,000 for first offense
   b. Up to $25,000 for second offense within 5 years
   c. Up to $50,000 for further violations in 7 years
5. Cases heard in federal court can result in the award of actual and unlimited punitive damages
6. Complaints brought under Civil Rights Act of 1866 taken directly to federal court

2. State and local enforcement agencies
   1. Many states and municipalities have their own fair housing laws
   2. All complaints filed with HUD are referred to local enforcement agencies if their laws are substantially equivalent with federal law
3. Threats or acts of violence - the Fair Housing Act protects those who seek or encourage the exercise of open housing rights

V. Closing the Real Estate Transaction

A. Pre-closing Procedures
   1. Consummation of the real estate transaction
      a. Promises made in sales agreement fulfilled
      b. Mortgage loan funds distributed
      c. Title transferred
   2. Buyer’s issues: the buyer will want to be assured that:
      a. The seller is delivering good title
      b. The property is in the promised condition. Inspecting:
         1). The title evidence
         2). The seller’s deed
         3). Any documents regarding removal of liens and encumbrances
         4). The survey
         5). The results of property inspection
         6). Any leases
   3. Final property inspection to make certain
      a. Necessary repairs made
      b. Property well maintained
      c. Fixtures are in place
      d. No unauthorized removals or alterations
   4. Survey
   5. Seller’s issues. The seller will want to be assured that:
      a. The buyer has obtained the stipulated financing
      b. The buyer has sufficient funds to complete the sale
   6. Title procedures
      a. The buyer needs to be assured that the seller’s property and title comply with the contract requirements
      b. The seller is usually required to show proof of ownership by producing current title evidence
      c. The title or abstract company usually makes two title searches
         1). The first shows the seller’s status as of the contract date
         2). The second is made for the date the deed is recorded
         3). The seller may be required to execute an affidavit of title. In areas where closed in escrow, not needed

B. Conducting the Closing
   1. Face-to-face closing - the gathering of the parties interested in the real estate transaction at which the promises made in the real estate sales contract are kept or executed
      a. Two closings can occur:
         1). The closing of the buyer’s loan
         2). The closing of the sales transaction
      b. May be held at:
         1). The title insurance company
         2). The lending institution
         3). One of the parties’ attorney’s office
         4). The broker’s office
         5). The county recorder (or other local recording official) office
         6). The escrow company
      c. May be attended by:
         1). The buyer
         2). The seller
         3). The real estate licensees (brokers and salespeople)
         4). The attorney(s) for the seller and the buyer
5). The representative of the involved lending institutions
6). The representative of the title insurance company
d. The closing agent or closing officer - the person who presides over the closing
e. The exchange; made when all parties satisfied that everything is in order

2. Closing in escrow
a. The method of closing in which a disinterested third party is authorized to act as the escrow agent and coordinate the closing activities
b. Because the escrow agent is placed in a position of trust, many states have laws regulating escrow agents and limiting who may serve in this capacity

3. IRS reporting - Form 1099-S
a. Contains the seller’s social security number, sales price, and the amount of property tax that was reimbursed to the seller by the buyer (seen as income by the IRS)
b. Must be filed by the closing agent. If this person does not, the responsibility rests on the mortgage lender or ultimately the brokers involved

4. Lender’s interest in closing - to protect its security interest in the property, the lender can require:
a. A title insurance policy
b. A fire and hazard insurance policy
c. A survey
d. A termite or other inspection report
e. A certificate of occupancy (for newly constructed buildings)
f. Reserve or escrow accounts for tax and insurance payments
g. Representation by its own attorney at closing

C. RESPA Requirements
1. Purpose
a. To provide consumers with greater and more timely information on the nature and costs of settlement
b. To eliminate “kickback” and other referral fees that tend to unnecessarily increase the costs of settlement

2. RESPA requirements must be complied with when the purchase of a one to four family residential unit is financed by a federally related new first mortgage loan
a. Made by a federally chartered lending institution
b. Made by an institution whose deposits are federally insured
c. FHA insured
d. VA guaranteed
e. Administered by HUD
f. Intended to be sold to Fannie Mae, Ginnie Mae, or Freddie Mac

3. Exceptions to the “new loan” requirement
a. Purchase money mortgages
b. Installment sales (land contracts)
c. Buyer’s assumption of existing mortgage
d. No exception if:
   1). The terms of assumed loans are modified
   2). Assumed loans for which the lender charges more than $50 for the assumption

4. Controlled business arrangements (CBAs) - affiliated firms offer package of services to consumers
a. The relationship between the firms must be disclosed in writing to consumers
b. Consumers must be free to obtain the services elsewhere
c. Fees are not exchanged among the affiliated companies simply for the referral of business

5. Disclosure requirements
a. The lender must give a copy of special informational HUD booklet to every person from whom they receive or for whom they process a loan application
b. Within three business days of the loan application, the lender must provide the borrower with a good faith estimate of the settlement costs the borrower is likely to incur
c. The loan closing information must be prepared on the Uniform Settlement Statement (HUD Form 1) and available for inspection at or before settlement
d. Kickbacks and referral fees
   1). Kickbacks and unearned referral fees are prohibited
   2). The payment or receipt of any fee or thing of value where no service is actually rendered is prohibited

D. Preparation of Closing Statements
1. How the closing statement works
   a. A debit is a charge (an expense)
   b. A credit is an amount entered in a person’s favor
2. The buyer’s debits and credits are totaled; when the credits are subtracted from the debits, the difference is the cash the buyer must bring to the closing
3. The seller’s debits and credits are totaled; when the debits are subtracted from the credits, the difference is the amount the seller will receive at closing
4. Expenses
   a. Broker’s commission
   b. Attorney’s fees
   c. Recording expenses
   d. Transfer tax
   e. Title expenses
   f. Loan fees
   g. Tax reserves and insurance reserves (escrow or impound accounts)
   h. Appraisal fees
   i. Survey fees
   j. Additional fees
E. Prorations - expenses divided between the seller and the buyer, including accrued items (such as real estate taxes) and prepaid items (such as fuel oil in a tank)
1. The arithmetic of prorating
   a. Four considerations
      1). The nature of the item being prorated
      2). Whether it is an accrued item requiring determination of earned amount
      3). Whether it is a prepaid item that requires the unearned amount refunded
      4). What arithmetic processes must be used
2. Accrued and prepaid items
   a. Accrued items = buyer credit
   b. Prepaid items = seller credit
3. General rules for calculating prorations
   a. The yearly charge is divided by a 360 day year (commonly called a banking year) or twelve months of 30 days each
   b. The yearly charge is divided by 365 (366 in a leap year) to determine the daily charge, then the actual number of days in the proration period is determined; and this number is multiplied by the daily charge
   c. Real estate taxes
      1). If they are paid in advance, the seller should be reimbursed for the portion of the year remaining after the buyer takes ownership
      2). If they are paid in arrears, the buyer is credited for the time the seller was occupying the property
   d. Mortgage loan interest – usually paid in arrears

**VI. Lending Calculations**
A. Loan-to-Value Ratios
B. Discount Points
C. Calculating Payments
D. Qualifying Buyers
E. Calculating Equity