



# **1** The Real Estate Business

## **REAL ESTATE PROFESSIONS**

### **Real estate activities**

- create, improve, manage, maintain, demolish, own, regulate, and transfer real properties

### **Property type specializations**

- residential; residential income; office; retail; industrial; farm and ranch; special purpose; land

## **REAL ESTATE BROKERAGE**

- procure a buyer or tenant for an owner or landlord, or vice versa

### **Forms of specialization**

- by property type; geographical area; type of transaction; type of client; by form of business organization; or by form of client relationship

### **Skills and knowledge**

- market conditions; law; financing; marketing; ethics; selling; communications; computer basics; and other skills

## **PROFESSIONAL ORGANIZATIONS**

- promote interests of practitioners and enhance their professional standing

## **REGULATION AND LICENSING**

### **Regulation of business practices**

- all facets of the industry are regulated by federal, state, and local laws; agents must understand relevant laws and adapt business practices accordingly

### **Real estate license laws**

- the primary body of laws and regulations governing the licensure and conduct of real estate brokers and agents
- license laws are administered and enforced under the jurisdiction of the state real estate commission

## **2** Rights and Interests in Real Estate

### **REAL ESTATE AS PROPERTY**

- Constitution guarantees private ownership of real estate; ownership rights not absolute; others may exert claims against one's property

### **Land**

- surface, all natural things attached to it, subsurface, and air above the surface; unique aspects: immobile, indestructible, heterogeneous

### **Real estate**

- land plus all permanently attached man-made structures, called improvements

### **Property**

- something that is owned by someone and the associated rights of ownership
- the bundle of rights: possession, use, transfer, exclusion, and encumbrance
- property is real or personal, tangible or intangible

### **Real property rights**

- any of the bundle of rights, applied to airspace (air rights), surface (surface rights), and subsurface (subsurface rights)

### **Water rights**

- Doctrine of Prior Appropriation: state controls water usage; grants usage permits
- littoral rights: abutting property owners own land to high water mark; may use, but state owns underlying land
- riparian rights: if navigable, abutting property owners own land to water's edge; may use, but state owns underlying land; if not navigable, owner owns land to midpoint of waterway

### **REAL VS PERSONAL PROPERTY**

- an item may be real or personal property depending on the "attachment" criterion and other circumstances

### **Fixtures**

- real property converted from personal property by attachment to real estate

### **Differentiation criteria**

- intention; adaptation; functionality; relationship of parties; contract provisions

### **Trade fixtures**

- personal property items temporarily attached to real estate in order to conduct business; to be removed at some point

### **Emblements**

- plants or crops considered personal property since human intervention is necessary for planting, harvesting

### **Factory-built housing**

- housing pre-built off-site; includes mobile homes; real or personal depending on attachment to land

### **Conversion**

- transforming real to personal property through severance, or personal to real property through affixing

### **REGULATION OF REAL PROPERTY INTERESTS**

#### **Federal regulation**

- grants overall rights of ownership; controls broad usage standards, discrimination

#### **State regulation**

- governs the real estate business; sets regional usage standards

#### **Local regulation**

- levies real estate taxes; controls specific usage

#### **Judicial regulation**

- applies case law and common law to disputes

# 3 Interests and Estates

## INTERESTS AND ESTATES IN LAND

- Interests**
  - any combination of bundle of rights
  - estates, encumbrances, police powers
- Estates in land**
  - include right of possession; also called tenancies
  - leaseholds: of limited duration
  - freeholds: duration is not necessarily limited
- FREEHOLD ESTATES**
  - implies "ownership" in contrast to leasehold
- Fee simple estate**
  - also "fee"; most common form of estate; not limited by one's lifetime
  - fee simple absolute: highest form of ownership interest
  - defeasible: can revert to previous owner for violation of conditions
- Life estate**
  - fee estate passes to another upon death of a named party
  - remainder: interest of a named party to receive estate after holder's death
  - reversion: interest of previous owner to receive estate after holder's death
- Conventional life estate**
  - full ownership interest, limited to lifetime of life tenant or another named party
  - created by agreements between parties
  - ordinary: on death of life tenant, passes to remainderman or previous owner
  - pur autre vie: on death of another; passes to remainderman or previous owner
- Legal life estate**
  - automatic creation of estate through operation of law
  - designed to protect family survivors
  - homestead: rights to one's principal residence
  - laws protect homestead from certain creditors
  - dower and curtesy: a life estate interest of a widow(er) in the real property
- LEASEHOLD ESTATES**
  - non-ownership possessory estates of limited duration
- Estate for years**
  - specific, stated duration, per lease
- Estate from period-to-period**
  - lease term renews automatically upon acceptance of monthly or periodic rent
- Estate at will**
  - tenancy for indefinite period subject to rent payment; cancelable with notice
- Estate at sufferance**
  - tenancy against landlord's will and without an agreement

# 4 Ownership

## SOLE OWNERSHIP

**Tenancy in severalty** ● sole ownership of a freehold estate

## CO-OWNERSHIP

● ownership by two or more owners

**Tenancy in common** ● co-tenants enjoy an individually owned, undivided interest; any ownership share possible; no survivorship

**Joint tenancy** ● equal, undivided interest jointly owned, with survivorship  
● requires four unities to create: time, title, interest, possession

**Tenancy by the entireties** ● equal, undivided interest jointly owned by husband and wife

**Community property** ● per state law, joint ownership of property by spouses as opposed to separate property  
● separate: acquired before marriage or by gift or inheritance

**Tenancy in partnership** ● ownership by business partners

## TRUSTS

● property granted by trustor to fiduciary trustee for benefit of beneficiary

**Living trust** ● personal and real property ownership created to take effect during one's lifetime (living trust) or after one's lifetime (testamentary)

**Land trust** ● real property ownership where grantor and beneficiary are same party; beneficiary uses, controls property, does not appear on public records

## OWNERSHIP BY BUSINESS ENTITIES

**Corporation** ● owned by stockholders; board of directors, officers, directors run business; liability of shareholders limited to value of shares; may own real estate in severalty or tenant in common

**Partnership** ● two or more partners; in general partnership, all partners run business and share liability; in limited partnership, general partners run business and are liable, limited partners liable only to the extent of their investment; both types may own real estate

**Limited liability company** ● members liability limited like in corporation, management flexible, income passed through and taxed as personal income; may own real estate

**CONDOMINIUMS** ● freehold ownership of a unit of airspace plus an undivided interest in the common elements as tenant in common with other owners

● may be sold, encumbered or foreclosed without affecting other unit owners

● creation: by developer's declaration

**COOPERATIVES** ● ownership of shares in owning corporation, plus proprietary lease in a unit; corporation has sole, undivided ownership

**TIME SHARES** ● a lease or ownership interest in a property for the purpose of periodic use by the owners or tenants on a scheduled basis

# 5

## Encumbrances and Liens

- ENCUMBRANCES** • non-possessory interests limiting the legal owner's rights
- EASEMENTS** • a right to use portions of another's property
- Easement appurtenant** • dominant tenement's right to use or restrict adjacent servient tenement; attaches to the real estate
- easement by necessity: granted by necessity, e.g. to landlocked owners
- party wall: negative easement in a shared structure
- Easement in gross** • a right to use property that does not attach to the real estate
- personal: not revocable or transferrable; ends upon death of easement holder
- commercial: granted to businesses; transferrable
- Easement creation** • voluntary grant, court decree by necessity or prescription, eminent domain
- by prescription: obtainable through continuous, open, adverse use over a period
- Easement termination** • release; merger; abandonment; condemnation; change of purpose; destruction; non-use
- ENCROACHMENTS** • intrusions of real estate into adjoining property; can become easements
- LICENSES** • personal rights to use a property; do not attach; non-transferrable; revocable
- DEED RESTRICTIONS** • conditions and covenants imposed on a property by deed or subdivision plat
- LIENS** • claims attaching to real and personal property as security for debt
- Lien types** • voluntary and involuntary; general and specific; superior and junior
- Lien priority** • rank ordering of claims established by lien classification and date of recording; determines who gets paid first if lienee defaults
- Superior liens** • rank over junior liens; not ranked by recording date; real estate tax and assessment liens and inheritance taxes
- Junior liens** • rank by recording date: judgment; mortgage, vendor's, utility, mechanic's, broker's, other tax liens; mechanic's lien priority "dates back" to when work or sale transpired
- FORECLOSURE** • enforcement of liens through liquidation or transfer of encumbered property
- Mortgage lien foreclosure** • liquidation or transfer of collateral property by judicial, non-judicial, or strict foreclosure
- Judicial foreclosure** • lawsuit and court-ordered public sale; deficiency judgments, redemption rights
- Non-judicial foreclosure** • "power of sale" granted to lender; no suit; no deficiency judgment; no redemption period after sale
- Strict foreclosure** • court orders legal transfer of title directly to lender without public sale
- Deed in lieu of foreclosure** • defaulted borrower deeds property to lender to avoid foreclosure
- Short sale** • sale at a price that does not cover a borrower's loan balance

# **6** Transferring and Recording Title to Real Estate

## **TITLE TO REAL ESTATE**

- Legal and equitable title**
  - legal title: ownership of the bundle of rights
  - equitable title: a conditional right to legal title subject to an owner's agreements with buyers and creditors
- Notice of title**
  - how ownership is evidenced to the public
  - actual notice: knowledge acquired or imparted directly through demonstrable evidence, e.g., presenting or inspecting a deed, visiting a party in possession
  - constructive notice: knowledge one could or should have obtained, as presumed by law; imparted by recording in public records "for all to see"
- Transferring title**
  - voluntary by grant, deed, or will
  - involuntary by descent, escheat, eminent domain, foreclosure, adverse possession, estoppel
- DEEDS OF CONVEYANCE**
  - instruments of voluntary conveyance by grantor to grantee
- Delivery and acceptance**
  - legal title transfers upon competent grantor's intentional delivery and grantee's acceptance; in Torrens, title transfers upon registration
- Validity**
  - grantor, grantee, in writing, legal description, granting clause, consideration, grantor's signature, acknowledgement, delivery and acceptance
- Deed clauses and covenants**
  - premises clause: granting
  - habendum clause: type of estate
  - reddendum clause: restrictions
  - tenendum clause: other property included
  - warrants: seizen; quiet enjoyment; further assurance; forever; encumbrances; grantor's acts
- Statutory deeds**
  - bargain and sale: "I own but won't defend"
  - general warranty: "I own and will defend"
  - special warranty: "I own and warrant myself only"
  - quitclaim: "I may or may not own, and won't defend"
- Special purpose deeds**
  - used for different purposes, to convey certain interests, or by certain parties
- Transfer tax**
  - state tax on conveyances based on price
- WILLS**
  - last will and testament: voluntary transfer to heirs after death
  - maker: devisor or testator; heir: devisee; estate: devise
- Types of will**
  - witnessed; holographic; approved; nuncupative
- Validity**
  - adult; competent; indicates "last will and testament"; signed; witnessed; voluntary
- Probate**
  - if testate, estate passes to heirs; if intestate, to successors by descent; if intestate with no heirs, estate escheats to state or county
  - process: validate will; validate, settle claims and pay taxes; transfer balance of estate to heirs

# 7 Real Estate Leases

- THE LEASE CONTRACT**
- instrument of leasehold conveyance; contract of covenants and obligations
  - landlord grants temporary, exclusive use in trade for rent and reversion
- Leasehold rights and obligations**
- tenant rights: exclusive use and possession; quiet enjoyment; profits
  - tenant obligations: pay rent; maintain premises; follow rules
  - landlord rights: receive rent; repossess; monitor property condition
  - landlord obligations: support and services; maintenance
  - leasehold rights survive death and conveyance or encumbrance
- Contract requirements**
- parties; legal description; exclusive possession; legal use; lease term; consideration; offer and acceptance; signatures; written if over one year in term
- Lease clauses**
- rent; deposit; term; repairs and maintenance; subletting and assignment; rules and regulations; improvements; alterations; options; damage; destruction
- TYPES OF LEASE**
- based on expense responsibility; how rent is paid; property type; rights leased
- Gross lease**
- landlord pays expenses; tenant pays more rent
- Net lease**
- tenant pays some or all expenses; rent is less
- Percentage lease**
- landlord receives rent minimum plus percentage of retailer's sales
- Residential lease**
- gross lease hybrid; short term; uniform terms reflect landlord-tenant standards
- Commercial lease**
- longer term; entails tenant improvements; complex, negotiable lease terms
- Ground lease**
- landlord owns and leases ground but does not own improvements
- Proprietary lease**
- for cooperative unit owners; indefinite term; assigned to new unit owner on sale
- Leasing of rights**
- leasehold transfer of rights for limited use; examples: air, mineral, water rights
- DEFAULT AND TERMINATION**
- Remedies for default**
- sue for damages, lease cancellation, and/or specific performance
- Default by tenant**
- cancellation; damages; suit for possession; must give proper notice
- Default by landlord**
- suit for constructive eviction; must vacate premises to uphold
- Causes for lease termination**
- default; term expiration; notice; voluntary agreement; property destruction; condemnation; death, in some cases; abandonment
- UNIFORM RESIDENTIAL LANDLORD AND TENANT ACT**
- aims to balance landlord and tenant rights; to standardize leases and eviction procedures; to protect tenants; serve as model for state-level legislation
- Areas of regulation**
- contract language; waiver of rights; deposit; obligations of landlord and tenant; default and eviction

**INVOLUNTARY  
TITLE TRANSFER**

- descent and escheat: no will
- foreclosure: lose title by forfeiture
- eminent domain: lose title to public for the greater good
- adverse possession: by claim of right or color of title; continuous, notorious, hostile possession; may have to pay taxes
- estoppel: barred by prior acts or claims

**TITLE RECORDS**

- all instruments affecting title must be recorded
- give public notice; protect owners; protect lienholders' claims

**Chain of title**

- successive property owners from original grant to present owner
- abstract of title: chronology of recorded owners, transfers, encumbrances

**Recording system**

- local property recording system governed by state law
- Torrens registry: requires court action initially: legal title does not pass until recordation occurs

**Title evidence**

- needed to prove marketable title as well as who owns
- forms of evidence: Torrens; title insurance; attorney's opinion of abstract; title certificates



# 8 Land Use Planning and Control

## REAL ESTATE PLANNING

### Goals of land use control

- preserve property values; promote highest and best use; safeguard public health, safety and welfare; control growth; incorporate community consensus
- process: develop plan; create administration; authorize controls

### The master plan

- long term growth and usage strategies; often required by state law
- local plans fuse municipal goals and needs with state and regional laws

### Planning objectives

- control growth rates: how much growth will occur and at what rate
- control growth patterns: type of growth desired, where it should be located
- accommodate demand for services and infrastructure

### Plan development

- research trends and conditions; blend local and state objectives into master plan

### Planning management

- commission makes rules, approves permits, codes, and development plans

## PUBLIC LAND USE CONTROL

### Zoning

- "police power" granted by state-level enabling acts; zoning ordinance: creates zones, usage restrictions, regulations, requirements

### Types of zone

- residential, commercial, industrial, agricultural, public, PUD

### Zoning administration

- Zoning Board of Adjustment oversees rule administration and appeals
- nonconforming use: legal if use prior to zone creation; variance: exception based on hardship; special exception: based on public interest; amendment: change of zones; rezoning

### Subdivision regulation

- plat of subdivision and relevant requirements must be met and approved; must meet FHA requirements for insured financing

### Building codes

- comprehensive onsite and offsite construction and materials standards; must be met to receive certificate of occupancy

### Public acquisition and ownership

- eminent domain: public power to acquire property for public use

## PRIVATE LAND USE CONTROL

### Deed restriction

- single-property use restriction as stipulated in a deed; may not be discriminatory

### Declaration restriction

- use restriction in multiple-property declarations; enforced by court injunction

### Deed condition

- usage restriction that can trigger repossession by a previous owner if violated

### HOA regulation

- homeowner's association rules require conformity to CCRs

## ENVIRONMENTAL CONTROLS

### Areas of concern

- air, soil, water quality; ambient health hazards; natural hazards

### Major legislation

- limits damage to environment; standards for air, land, water, materials use

### Responsibilities & liabilities

- disclosure and information for practitioners; remediation for owners; lead disclosure; CERCLA/Superfund exposure; Phase I, II, III Environmental Site Assessments to detect and mitigate contamination

# 9 Legal Descriptions

## **METHODS OF LEGAL DESCRIPTION**

- metes and bounds; rectangular survey system or government survey; recorded plat or lot and block
- legal description is sufficiently accurate, acceptable in court of law; facilitates transfers; avoids disputes; used in legal contracts

## **METES AND BOUNDS**

- describes property perimeter by landmarks, monuments, distances, angles
- from point of beginning (POB), describes perimeter and returns to POB; usable within rectangular survey system

## **RECTANGULAR SURVEY SYSTEM**

### **The survey grid**

- meridians: north-south lines six miles apart
- parallels: east-west lines six miles apart
- ranges: north-south strips of area between meridians; tiers: east-west strips of area between parallels; townships: the area representing the intersection of a range and a tier, consisting of six-mile by six-mile squares of land

### **Sections of a township**

- 36 sections per township, each one-mile square (1 mile on each side)

### **Fractions of a section**

- 1 section = 640 acres; fractions of sections described by size and location within progressively larger quarters of section

### **Converting section fractions to acres**

- formula: multiply denominators of section fractions; divide product into 640

## **RECORDED PLAT METHOD**

- or lot and block system; used in surveyed subdivisions

### **Subdivision plat map**

- surveyed plat of subdivided tract; legal descriptor if approved and recorded

### **Description format**

- lots within subdivision are identified by lot reference and block reference: "Lot 7 Block B of the Grand Oaks Subdivision"

## **DESCRIBING ELEVATION**

- datum: a standard elevation reference point; benchmark: elevation marker officially surveyed and registered

# 10 Real Estate Contract Law

## CONTRACT VALIDITY AND ENFORCEABILITY

### Legal status of contracts

- contract: mutual promises based on "meeting of the minds" to do or refrain from doing something; potentially enforceable if created validly
- valid: meets criteria
- void: does not meet criteria
- voidable: invalid if disaffirmed
- valid yet unenforceable: certain oral contracts

### Criteria for validity

- competent parties; mutual consent; valuable consideration; legal purpose; voluntary, good faith act

### Validity of a conveyance contract

- must be in writing; contain a legal description; be signed by one or more parties

### Enforcement limitations

- statute of frauds: must be written to be enforceable
- statute of limitations: must act within time frame

### Electronic contracting

- federal law: electronic records and signatures are legal and must be accepted; enforceable regardless of medium

## CONTRACT CREATION

### Offer and acceptance

- valid offer and valid acceptance creates contract
- offer becomes contract on communication of acceptance by offeree to offeror

### Counteroffer

- any offer in response to an offer or any altered original offer; nullifies original offer

### Revocation of an offer

- offeror may revoke offer prior to communication of acceptance by offeree

### Termination of an offer

- acceptance; rejection; revocation; expiration; counteroffer; death or insanity

### Assignment of a contract

- assignable unless expressly prohibited or a personal service

### Contract preparation

- restricted unless licensed as attorney or a party to the contract

## CLASSIFICATIONS OF CONTRACTS CONTRACT TERMINATION

### Forms of contract termination

- performance; infeasibility; mutual agreement; cooling-period rescission; revocation; abandonment; lapse of time; invalidity of contract; breach of contract

### Breach of contract

- default without cause
- legal remedies: rescission; forfeiture; suit for damages; specific performance

# 11

## Agency

### THE AGENCY RELATIONSHIP

#### Basic roles

- principal, or client, hires agent (broker) to find a ready, willing, and able customer (buyer, seller, tenant); client-agent fiduciary foundations: trust, confidence, good faith

#### Types of agency

- universal: represent in business and personal matters; can contract for principal
- general: represent in business matters; agent can contract for principal
- special: represent in single business transaction; normally agent cannot contract for principal; the brokerage relationship is usually special agency

#### Creating an agency relationship

- created by express written or oral agreement or as an implied agreement by actions of either party

#### Terminating an agency relationship

- causes: fulfillment; expiration; mutual agreement; incapacity; abandonment; or destruction of property; renunciation; breach; bankruptcy; revocation of license

### FIDUCIARY DUTIES

#### Agent's duties to the client

- skill, care, diligence; loyalty; obedience; confidentiality; disclosure; accounting

#### Agent's duties to the customer

- honesty and fair dealing; exercise of reasonable care and skill; proper disclosures; danger areas: misrepresentation; advising beyond expertise

#### Principal's duties

- availability; provide information; compensation

#### Breach of duty

- liabilities: loss of listing, compensation, license; suit for damages

### FORMS OF REAL ESTATE AGENCY

#### Single agency

- seller agency; buyer agency; tenant representation

#### Subagency

- outside brokers and agents who help listing agent; listing broker's own agents

#### Dual agency

- representing both sides; potential conflict of interest; must disclose, obtain written consent; types: voluntary by consent; involuntary by actions of parties (implied agency); duties: all but full disclosure and loyalty

#### Designated agency

- an agent is designated to represent a client exclusively; no other licensees in the firm have any agency relationship with the client unless named in the agreement

#### No agency

- "facilitator" or "transaction broker"; representing neither party in the transaction; duties to both parties: accounting; skill, care and diligence; honesty and fair dealing; disclosures affecting property value

### AGENCY DISCLOSURE

#### Objectives of disclosure

- declare; explain; offer choice; obtain documented consent

#### Seller agent disclosures

- to client: in writing on or before listing is executed; to customer: prior to substantive contact, in writing; oral permitted but must have written follow-up

#### Buyer agent disclosures

- in writing; upon first contact with listing agent or seller

#### Dual agent disclosures

- "informed, written consent"; may not disclose: price or financing positions or motivations unless authorized

#### Facilitator disclosures

- on becoming transaction broker or on substantive contact whichever is first

# 12 Listing Agreements

## REVIEW OF LEGAL FOUNDATIONS

### Agency law

- listing: broker's enforceable contract of employment with client establishing special agency relationship to procure a customer
- parties: listing broker and client; broker's subagents; customers and prospects
- fiduciary duties: loyalty; obedience; disclosure; care; diligence; accounting
- scope of authority: listings are special or limited agency, not general agency agreements; broker may not contract for client unless specifically authorized; clients liable only for broker's acts within scope of authority

### Contract law

- listings are unilateral contracts; listing must be valid to be enforceable; legal form: oral listings are valid and enforceable except, in many states, exclusive right-to-sell listings which must be written to be enforceable
- listings are not assignable since they are personal service contracts

## TYPES OF LISTING AGREEMENT

### Exclusive right-to-sell (or lease)

- owner listing: authorization to sell or lease; buyer or tenant listing: authorization to represent buyer or tenant
- most prevalent; given to one broker; must usually be written; must expire; broker gets commission if property transfers during period

### Exclusive agency

- exclusive excepting owner; oral or written; must expire; broker gets commission unless owner sells

### Open listing

- non-exclusive; oral or written; no stated expiration; procuring cause gets commission; no commission if client procures customer

### Net listing

- all sale proceeds above a seller's minimum price go to the broker; discouraged, if not illegal

### Buyer and tenant agency agreements

- open or exclusive listings with buyers or tenants to represent their interests compensation in form stipulated by agreement; may be paid by seller or landlord at closing; payable if buyer defaults; agent has fiduciary and disclosure duties

### Transaction broker agreements

- non-agency; no fiduciary duties; agent does not work in the interests of or for the benefit of either party

### Multiple listing

- listing placed in MLS; owners consent to rules and provisions of MLS

### Limited services agreement

- agreement that commits licensee to provide a limited, specified list of services to a client instead of the full set due under a standard agreement

## FULFILLMENT AND TERMINATION

### Agent's performance

- based on results: find ready willing and able customer or effect a sale; may perform only authorized tasks to achieve result; must verify owner and property data; may delegate duties to salespeople and other brokers

### Compensation

- negotiated; where disputed, procuring cause is owed commission

### Causes for termination

- performance; infeasibility; mutual agreement; revocation; abandonment; breach; expiration; invalidity; incapacitation or death; involuntary transfer; destruction of property

**Revoking a listing**

- clients always have power to revoke during period, but may incur liability for commission or damages

**LISTING AGREEMENT CLAUSES****Exclusive right-to-sell clauses**

- minimal requirements: broker's and owners' names; address and/or legal description; listing price; expiration date; agent's duties; compensation terms; authority granted; agency and non-agency disclosures: seller's representations and condition disclosures

**Exclusive buyer agency clauses**

- minimal requirements virtually identical to exclusive right-to-sell; distinguishing features: buyer's representation of exclusivity; agent compensation; buyer's acknowledgment of other buyers

**Transaction broker clauses**

- may be exclusive or non-exclusive; typical principle provisions: identification of parties and property; agent's authorized activity; declaration of non-agency; broker's duties; buyer's acknowledgment of other buyers; compensation; buyer or seller duties; expiration date

# 13 The Brokerage Business

## FUNCTION AND ORGANIZATION

### The core activity of brokerage

- procuring buyer, seller, tenant, or leased property for a client, often with the help of other brokers and a multiple listing service
- skills: listing, marketing, facilitating, managing information
- Multiple Listing Service: network of brokers who share listings

### Who may legally broker real estate?

- yes: sole proprietorship, for-profit corp., general or limited partnership, joint venture. no: non-profit corp., business trust, cooperative association

### Types of brokerage organization

- independents; franchises; agencies by property type, by transaction type, and by client type; limited and full service agencies

## THE BROKER-SALESPERSON RELATIONSHIP

### Legal relationships

- salesperson is agent, fiduciary of broker; acts in broker's name; subagent of client
- **may not:** have two employers; be paid by other parties; bind clients contractually

### Salesperson's employment status

- may be employee or contractor; relationship defined by agreement; assistant may be licensed or unlicensed; if licensed, supervised and paid by employing broker

### Obligations and responsibilities

- agent to broker: obtain & sell listings; follow policies and employment provisions; promote ethics and broker's reputation
- broker to agent: provide data, office support, compensation, training; uphold ethics, policies, and employment agreement

### Agent compensation

- commissions per schedule after splits with cooperating brokers

## OPERATING A REAL ESTATE BROKERAGE

### Obtaining listings

- generate prospects; develop price range; complete listing presentation; negotiate execute and agreement

### Marketing listings

- develop marketing plan; sell and qualify prospective buyers; complete necessary disclosures; obtain offers

### Pre-closing activities

- facilitate fulfillment of contract contingencies and provisions
- no commingling or conversion of escrow funds

### Handling trust funds

- trust funds to be held in trust account in state- or federally-chartered institution; no commingling or conversion; timely deposit and withdrawal; full accounting

### Communications and technology

- marketing techniques using technology: broker cooperation via MLS and competitors' websites; email and texting; social media websites; smartphone communication capabilities; all must be used carefully and in conformity with advertising rules and other laws

### Managing information

- property data; buyer and tenant files; market data files

- Policy manual**
  - written procedures **and** policies on all aspects of the business to ensure smooth, consistent operations
- Advertisement regulations**
  - no misleading ads; must contain broker's ID; broker responsible for content; no blind ads
- Anti-trust laws**
  - Sherman Act and Clayton Act pioneered antitrust laws to prohibit unfair trade practices, trade restraints, and monopolies
  - illegal to collude, disadvantage competitors; fix prices; allocate markets; force tie-ins
- BUSINESS BROKERAGE**
  - sale of existing business and its real estate; opportunity and enterprise brokerage
- Business brokerage vs. real estate brokerage**
  - special skills: transaction knowledge; accounting; determining the price
- Transaction knowledge**
  - types of sale: asset sale and stock sale
  - documents: sale contract; real estate sale contract or assignment; no-compete agreement; consulting agreement
- Accounting**
  - income, expenses, and profit
  - balance sheet: assets, liabilities, net worth
  - assets: tangible and intangible
  - goodwill: intangible asset--difference between price & other assets
- Determining a price**
  - reconciliation of income, cost, and market data approaches; influenced by risk and stability of future income
- Business brokerage regulation**
  - may need securities license; must comply with Bulk Sales law



# 14

## Contracts for the Sale of Real Estate

### CONTRACT FOR SALE

- Legal characteristics**
- binding, bilateral contract for purchase and sale; enforceable; executory, or to be fulfilled; expires upon closing; must be in writing; contain valuable consideration; identify property; be signed by all; be a valid contract
- Contract creation**
- by unqualified acceptance of an offer; gives buyer equitable title, power to force specific performance
- Earnest money escrow**
- secures contract validity and buyer's equitable interest; varies in amount; deposit controlled by disinterested party who must act according to escrow instructions
- Contract contingencies**
- conditions that must be met for the contract to be enforceable
- Default**
- buyer may sue for cancellation and damages or for specific performance; seller may claim deposit as liquidated damages, or may sue for cancellation, other damages, or for specific performance

### SALE CONTRACT PROVISIONS

- Primary provisions**
- parties, consideration, legal description, price and terms, loan approval, earnest money, escrow, closing and possession dates, conveyed interest, type of deed, title evidence, property condition warranty, closing costs, damage and destruction, default, broker's representation, commission, seller's representations
- Secondary provisions**
- inspections, owner's association disclosure, survey, environmental hazards, compliance with laws, due-on-sale, seller financing disclosure, rental property tenant's rights, FHA or VA financing condition, flood plain and flood insurance, condominium assessments, foreign seller withholding, tax-deferred exchange, merger of agreements, notices, time of the essence, fax transmission, survival, dispute resolution, addenda

### THE OPTION-TO-BUY CONTRACT

- optionor gives option to optionee; unilateral contract: seller must perform; buyer need not; if option exercised, option becomes bilateral sale contract
- Contract requirements**
- must include: non-refundable consideration for the option right; price and terms of the sale; option period expiration date; legal description; must be in writing and meet contract validity requirements
- Common clause provisions**
- special provisions: how to exercise option; terms of option money forfeiture; how option money will be applied to purchase price

### Legal aspects

- creates equitable interest; is assignable; should be recorded

### CONTRACT FOR DEED

- purchase price is paid over time in installments; seller retains title; buyer takes possession; at end of period, buyer pays balance of price, gets legal title
- Interests and rights**
- seller may encumber or assign interest; remains liable for underlying mortgage
  - buyer may use, possess, profit; must make periodic payments, maintain the property, and purchase at end of term
- Default and recourse**
- if seller defaults, buyer may sue for cancellation and damages or specific performance; seller's default remedies vary by area; may sue for specific performance or damages, or may need to foreclose

# 15

## Real Estate Market Economics

### THE MARKET SYSTEM

#### Supply and demand

- supply: goods or services available for sale, lease, or trade
- demand: goods or services desired for purchase, lease, or trade

#### Price and value

- price mechanism: quantified value of an exchange
- value components: desire; utility; scarcity; purchasing power

#### Productivity and costs

- cost plus profit equals minimum price; production cost possible component of value

#### Market interaction

- market: transaction arena where suppliers and demanders define value through the price mechanism
- if supply increases relative to demand, price decreases; if demand increases relative to supply, price increases

#### Market equilibrium

- supply and demand tend toward balance where they are equal
- market equilibrium: price, cost, value theoretically the same; market imbalances are caused by changes in supply or demand

### REAL ESTATE MARKET DYNAMICS

#### Economic characteristics of real estate

- governed by supply, demand, price, costs, value components, government influence
- inherent value; unique appeal; immovable supply; illiquid; slow response to cycles; decentralized market

#### Real estate supply and demand

- supply: property available for sale or lease; measured in dwelling units, square feet, acres; influenced by costs, finance, returns, government regulation
- demand: property buyers and tenants wish to acquire; measured in households, square feet, acres; influences: residential-- quality, amenities, price convenience; retail-trade area, sales, competition, site access, visibility; growth patterns; office--efficiency, costs, functionality; industrial-- functionality, labor, regulatory compliance, access to labor, supplies, distribution channels
- base employment, total employment, population determine overall demand
- if employment and population increase, demand and prices increase; if they decrease, the opposite occurs
- supply-demand indicators are price, vacancy, and absorption; vacancy is existing, unoccupied supply; absorption is the "filling up" of vacancy
- real estate supply-demand cycle: undersupply > accelerated construction adds supply > equilibrium > construction adds more supply > oversupply > construction stops > equilibrium > demand absorbs supply

#### Market influences on supply and demand

- local economic factors; national economic trends in money supply, inflation; government regulation at all levels

# 16

## Appraising and Estimating Market Value

- REAL ESTATE VALUE**
  - present monetary worth of benefits arising from ownership, including: income, appreciation, use, tax benefits
- Foundations of real estate value**
  - anticipation, substitution, contribution, change, highest and best use, conformity, supply, demand, progression, regression, assemblage, subdivision, utility, transferability
- Types of value**
  - market, reproduction, replacement, salvage, plottage, assessed, condemned, depreciated, reversionary, appraised, rental, leasehold, insured, book, mortgage
- APPRAISING MARKET VALUE**
- Market value**
  - price willing buyer and seller would agree on given: cash transaction, exposure, information, no pressure, arm's length, marketable title, no hidden influences
- The appraisal and its uses**
  - a professional's opinion of value, supported by data, regulated, following professional standards; used in real estate decision-making
- Measuring living area**
  - standards vary by locality; national guidelines from ANSI and Fannie Mae
- Steps in the appraisal process**
  - define purpose, collect and analyze data, identify highest and best use, estimate land value, apply basic appraisal approaches, reconcile, compile report
- SALES COMPARISON APPROACH**
  - most commonly used; relies on principles of substitution and contribution
- Steps in the approach**
  - compare sale prices, adjust comparables to account for differences with subject
- Identifying comparables**
  - must be physically similar, in subject's vicinity, recently sold in arm's length sale
- Adjusting comparables**
  - deduct from comp if better than subject; add to comp if worse than subject
- Weighting adjustments**
  - best indicator has fewest and smallest adjustments, least net adjustment from the sale price
- Broker's comparative market analysis**
  - abridged sales comparison approach by brokers and agents to find a price range
- COST APPROACH**
  - most often used for recently built properties and special-purpose buildings
- Types of cost appraised**
  - reproduction: precise duplicate; replacement: functional equivalent
- Depreciation**
  - loss of value from deterioration, or functional or economic obsolescence
- Steps in the approach**
  - land value plus depreciated reproduction or replacement cost of improvements
- INCOME APPROACH**
  - used for income properties and in a rental market with available rental data
- Steps in the approach**
  - value = NOI divided by the capitalization rate
- GRM and GIM approach**
  - GRM: price divided by monthly rent; value: GRM times monthly rent; GIM: price divided by gross annual income; value: GIM times annual income
- REGULATION OF APPRAISAL**
- Licensure**
  - state-licensed or -certified per FIRREA/USPAP for federally-related appraisals
- Professional standards**
  - USPAP establishes appraisal standards, guidelines and provisions
- Professional associations and designations**
  - founders of Appraisal Foundation offer education and professional designations

# 17

## Real Estate Finance

### **ANATOMY OF MORTGAGE LENDING**

#### **Mechanics of a loan transaction**

- mortgage financing: using borrowed money secured by a mortgage to finance the purchase of real estate
- instruments: note and mortgage or trust deed
- mortgage mechanics: borrower gives lender note and mortgage; lender gives borrower funds and records a lien
- trust deed mechanics: trust deed conveys title from the borrower/trustor to a third-party trustee who holds title on behalf of the lender/beneficiary until the debt is repaid

#### **Financial components of a loan**

- original principal: capital amount borrowed on which interest payments are calculated
- loan balance: remaining unpaid principal at any point in the life of the loan
- interest: charge for the use of money; rate fixed or variable
- Annual Percentage Rate (APR) includes interest and all other finance charges; lender must disclose on residential properties
- point: one percent of the loan amount, charged by lender at origination to obtain required return
- term: period of time for repayment of interest and principal
- payment: the periodic payment of interest and/or principal

#### **Promissory note**

- legal instrument executed by borrower stating debt amount, loan term, method and timing of repayment, interest rate, promise to pay; may repeat other provisions from mortgage document or deed of trust; negotiable instrument assignable to a third party

#### **Mortgage document and trust deed**

- the legal documents which pledge the property as collateral for the loan
- may include clauses covering payment of principal and interest, prepayment, late charges, escrow for taxes and insurance, liens, insurance requirements, occupancy and maintenance, lender's rights, private mortgage insurance, inspection, and other conditions of performance

### **INITIATING A MORTGAGE LOAN**

#### **The loan application**

- borrower provides personal and property data; supporting documentation: appraisal report, credit report, purchase contract, income and/or employment verification
- lenders must accept all completed applications and notify applicants about disposition of application

#### **Mortgage loan underwriting**

- process of evaluating borrower's ability to repay and value of the property
- loan-to-value ratio: relationship of loan amount to property value, expressed as a percentage

## QUALIFYING FOR A MORTGAGE LOAN

### Equal Credit Opportunity Act

- lender must evaluate applicant according to applicant's own income and credit information

### Income qualification

- income ratio and debt ratio qualify borrower's income; income ratio applied to gross income determines housing expense maximum; debt ratio takes revolving debt into account

### Loan constant

- monthly or annual payment amount needed to amortize a \$1,000 loan given interest rate and term; used to derive loan amount or payment amount with known interest rate and loan term

### Cash qualification

- lender verifies applicant's sources of cash for down payment; extra cash enhances income qualification evaluation

### Net worth

- extent to which applicant's assets exceed liabilities as a further source of reserves

### Credit evaluation

- lender obtains credit reports to evaluate applicant's payment behavior

### Loan commitment

- written pledge by lender to grant loan under specific terms; firm, lock-in, conditional, take-out

### CLOSING A LOAN

- usually simultaneous with closing of real estate transaction; transfer of funds, signing of documents, escrow deposits

## LAWS AFFECTING MORTGAGE LENDING

### Truth-in-Lending and Regulation Z

- Reg Z implements Truth-in-Lending Simplification and Reform Act and Consumer Credit Protection Act
- provisions: lender must disclose finance charges and APR prior to closing; borrower has limited right of rescission; lender must follow disclosure requirements in advertising

### Equal Credit Opportunity Act

- ECOA prohibits discrimination in lending

### Real Estate Settlements and Procedures Act

- RESPA standardizes settlement practices
- provisions: lender must provide CFPB booklet explaining loans, settlement costs and procedures; lender must provide CFPB Loan Estimate of settlement costs within three days of application; lender must provide CFPB Closing Disclosure three days before loan consummation

### National Flood Insurance Act

- borrowers of "federally-related loans" must obtain flood insurance if property is in designated flood-hazard area

## THE MORTGAGE MARKET

### Supply and demand for money

- relationship between money supply and demand affects interest rates, consumer prices, availability of mortgage money
- Federal Reserve controls: T-bills; reserve requirement, discount rate

### The primary mortgage market

- originates mortgage loans directly to borrowers; savings and loans, commercial banks, mutual savings banks, life insurance companies, mortgage bankers, credit unions

**The secondary mortgage market**

- buys existing loans to provide liquidity to primary lenders; Fannie Mae, Ginnie Mae, Freddie Mac, investment firms, life insurance companies, pension funds

**Role of FNMA, GNMA, FHLMC, and FAMC**

- FNMA buys conventional, FHA- and VA-backed loans and pooled mortgages; guarantees payment on mortgage-backed securities; GNMA guarantees payment on certain types of loans; FHLMC buys and pools mortgages; sells mortgage-backed securities; FAMC funds agricultural assets, businesses and related capital requirements for the farming community

**TYPES OF REAL ESTATE LOANS**

**Conventional loans**

- permanent, long-term loans not insured by FHA or guaranteed by VA

**FHA-insured loans**

- insured loans granted by FHA-approved lenders to borrowers who meet FHA qualifications

**VA-guaranteed loans**

- guaranteed loans granted by VA-approved lenders to qualified veterans

**Common loan structures**

- amortizing, negative amortizing, interest only, fixed rate, adjustable rate, senior, junior, fixed or graduated payment, balloon, buydown

**Seller financing**

- purchase money mortgages: loans by the seller to the property buyer for all or part of the purchase price; contract for deed: installment sale where seller finances buyer and retains title until contract terms are met

**Special-purpose loans**

- home equity, package, construction, bridge, equity participation, take-out, reverse annuity, and blanket

**INVESTMENT  
FUNDAMENTALS****Investment  
characteristics**

- the greater the risk, the higher the expected return
- some investments require more investor involvement than others
- some investments are more liquid (convertible to cash) than others

**Rewards**

- investors seek to increase wealth through income, appreciation, leverage and tax benefits

**Risks**

- risks: changes in supply and demand for the investment (market risk), changes in businesses with which the investment is connected (business risk), changes in the value of money (purchasing power risk), and changes in interest rates (financial risk)

**Types of investments**

- among the investor's choices are investments in money (e.g., certificates of deposit), equity (e.g., stocks), debt (e.g., bonds and mortgages), and real estate (income and non-income properties)

**REAL ESTATE  
AS AN INVESTMENT****Risk and reward**

- the real estate investor must weigh the potential risks and returns inherent in market variability, expected vs. real income, use of borrowing leverage, changes in tax treatment of capital gains and income, and the cost of capital

**Illiquidity  
Management  
requirements**

- real estate is generally less liquid than other investment types: it takes time to market a property
- real estate tends to require more investor involvement than other investments do: maintenance, management, operation

**REAL ESTATE  
INVESTMENT ENTITIES****Direct**

- buying a property and taking responsibility for management and operation

**Syndicate and  
partnership**

- a group of investors pool resources to buy, develop and/or operate a property

**Real Estate  
Investment Trust**

- REIT: investors buy certificates in a trust that invests in mortgages or real estate and receive income according to shares owned

**Real Estate Mortgage  
Investment Conduit**

- REMIC: investors hold residual or regular interests in an entity that holds a pool of mortgages secured by real property

**TAXATION OF REAL  
ESTATE INVESTMENTS****Taxable income**

- gross income received minus allowable expenses, deductions and exclusions

**Cost recovery**

- deduction of a portion of a property's value from gross income each year over the

**Gain on sale**

- an excess of proceeds from sale of a property over the original cost of the property, subject to adjustments

**Interest**

- mortgage interest is deductible from annual gross income from a property, subject to limitations

**Passive activities**

- business activities in which the taxpayer does not materially participate, including interests in limited partnerships and rental activities; losses from such activities can be used to offset income from other passive activities

## **INVESTMENT ANALYSIS OF A RESIDENTIAL PROPERTY**

### **Appreciation**

- increase in the value of an asset over time; may be stated as a difference between the original price and current market value, or as a percentage increase over the original price; not a true measure of investment return

### **Deductibles**

- for non-income properties, primary tax benefit is annual deduction for mortgage

### **Tax liability**

- the seller of a principle residence owes tax on any capital gain that results from the sale unless excluded; capital gain is defined as the amount realized minus the adjusted basis

### **Gains tax exclusion**

- up to \$250,000 for a single seller and \$500,000 for a married couple can be excluded from gains tax every two years

## **INVESTMENT ANALYSIS OF AN INCOME PROPERTY**

### **Pre-tax cash flow**

- annual pre-tax cash flow is net operating income minus debt service

### **Tax liability**

- tax liability on income from a property is based on taxable income: net operating income minus interest expense and cost recovery

### **After-tax cash flow**

- annual after-tax cash flow is pre-tax cash flow minus tax liability

### **Investment performance**

- a few common measures of investment performance are:
  - return on investment (net operating income divided by price)
  - cash-on-cash return (cash flow divided by cash invested)
  - return on equity (cash flow divided by equity)
  - discounted cash flow analysis
  - internal rate of return



# 19

## Real Estate Taxation

- TAXING ENTITIES**
- no federal ad valorem taxes, only federal tax on income and gain; federal government can impose a tax lien against real property
- State government**
- states may levy property taxes but many delegate this power to county and local government; states can impose a tax lien against real property
- County and local government**
- counties, cities, municipalities, townships and special tax districts levy taxes on real property
- Tax districts**
- established to collect funds for providing specific services, e.g., schools, fire protection, parks, community colleges, libraries, road maintenance
- AD VALOREM TAXATION**
- property tax levied annually on the taxable value of a property in order to help fund government and public services
- Tax base totalling**
- tax base equals the total of assessed values of all real property within the area, excluding exemptions
- Homestead exemption**
- a tax exemption of a portion of the assessed value of a property owned and occupied as a family home
- Other exemptions**
- immune from tax: government-owned properties; exempt from taxes: properties owned by non-profit-organizations
- Tax rate derivation**
- (1) taxing entity determines what budget requirements must be met by ad valorem tax; (2) divide tax requirement by the tax base
  - tax rate stated as mills (\$.001), or dollars per \$100 of assessed value, or dollars per \$1,000 of assessed value, or as a percentage of assessed value
- Tax billing and collection**
- individual tax bill: tax rate times taxable value
  - taxable value: assessed value minus exemptions and adjustments
- SPECIAL ASSESSMENTS**
- tax levied against specific properties that will benefit from a public improvement; amount is based on a pro rata share of the cost of the improvement and the value each parcel will receive from the improvement
- TAX LIEN ENFORCEMENT**
- Sale of tax certificates**
- the buyer of a tax certificate agrees to pay the taxes due and after a period of time may apply for a tax deed on the property
- Tax deed**
- conveys title in the tax sale
- Tax sale**
- the buyer must pay the taxes due, if still unpaid; the defaulted taxpayer may be able to redeem the property and reclaim title; if not redeemed, the state issues the tax deed to convey title to the buyer

# 20

## Professional Practices

- FAIR HOUSING LAWS**
  - enacted to create equal opportunity and access to housing and housing finance
  - state laws generally reflect federal fair housing laws; federal laws do not pre-empt local zoning laws but prohibit them from discriminating
- Civil Rights Act of 1866**
  - no discrimination in selling or leasing housing *based on race*
  - Executive Order 11063: no race discrimination involving FHA- or VA-backed loans
- Civil Rights Act of 1968**
  - Title VIII (Fair Housing Act): no housing discrimination *based on race, color, religion, national origin*
  - certain exceptions permitted
- Forms of illegal discrimination**
  - discriminatory misrepresentation, advertising, and financing; unequal services; steering; blockbusting; restricting access to market; redlining
- Title VIII exemptions**
  - privately-owned single-family with no broker and no discriminatory advertising; 1-4 unit apartment building where owner is resident and no discriminatory advertising; private club facilities leased to members; religious organization-owned facilities for members and no discrimination
- Jones v. Mayer**
  - no race discrimination, without exception
- Equal Opportunity in Housing Poster**
  - must be displayed by brokers
- Fair Housing Amendments Act of 1988**
  - no discrimination *based on sex or against the handicapped or families with children*
  - agent liable for complying with client's discriminatory acts
- Discrimination by the client**
- Violations and enforcement**
  - file HUD complaint, sue in court, or both; may obtain injunction, damages; violators subject to prosecution
- Fair financing laws**
  - Equal Credit Opportunity Act: no discrimination in housing finance based on race, color, religion, sex, marital status, age; Home Mortgage Disclosure Act: no redlining
- Americans with Disabilities Act**
  - no discrimination against those with disabilities; applies to employment, education, transportation, public facilities; equivalent access
  - Titles I (employment) and III (public accommodation) most common for real estate agents
- PROPERTY DISCLOSURES**
- Residential property condition**
  - written seller disclosure may be required; may or may not relieve agent of some liabilities
  - seller discloses known problems; agent discloses known material facts known or should have known; failure to disclose grants right of rescission to buyer
  - agent should advise seller of red flag issues detected; may include environmental concerns, property size and shape, neighborhood, construction quality, flooding, floorplan, adjacent property
- Environmental issues**
  - duties of detecting, disclosing, remediating for owner and agent vary; typically include: lead-based paint, mold, asbestos, air quality, water quality, carbon monoxide, septic system, drug manufacturing, radon, formaldehyde, underground tanks
  - agents need to be familiar with requirements of EPA, CERCLA/Superfund Act, Clean Air and Water Acts, Lead-based Paint Act, among others

	<ul style="list-style-type: none"> <li>licensees must be aware of issues, know where to find professional help, disclose</li> </ul>
<b>Warranties</b>	<ul style="list-style-type: none"> <li>agents should inform clients of limitations of home warranties; not a substitute for inspection</li> </ul>
<b>Inspections</b>	<ul style="list-style-type: none"> <li>inspections can reveal structural, electrical, plumbing, roof, foundation, pest, environmental issues; agent must disclose inspection results if known</li> </ul>
<b>Homeowners' Associations</b>	<ul style="list-style-type: none"> <li>agent must make sure existence, requirements, mandates, costs of homeowners' association are disclosed</li> </ul>
<b>OTHER PROFESSIONAL PRACTICES</b>	<ul style="list-style-type: none"> <li>codes of ethics provide self-regulating standards of conduct covering all facets of the profession; serve clients, customers, and the public; avoid sanctions and liability; cover practices such as job performance, duties to clients and customers, disclosures, non-discrimination, professional relationships</li> </ul>
<b>Job performance</b>	<ul style="list-style-type: none"> <li>maintain knowledge of market, laws, practices; recognize limits of agent's role</li> </ul>
<b>Duties to clients</b>	<ul style="list-style-type: none"> <li>fiduciary duties; truthful representation of facts; respect client relationships; submit offers; avoid illegal practices; document transaction</li> </ul>
<b>Duties to customers</b>	<ul style="list-style-type: none"> <li>truthful representation of facts; truthful advertising</li> </ul>
<b>Disclosure</b>	<ul style="list-style-type: none"> <li>compensating parties; property defects; agent's interest in property; use of client funds; agent's identity in advertising</li> </ul>
<b>Wholesaling</b>	<ul style="list-style-type: none"> <li>acting as an intermediary in a transaction by contracting to purchase, assigning the contract to another buying, and taking the difference as a fee; licensing may or may not be required</li> </ul>
<b>Love letters</b>	<ul style="list-style-type: none"> <li>personal notes from buyers to sellers to enhance attractiveness of an offer</li> </ul>
<b>Non-discrimination</b>	<ul style="list-style-type: none"> <li>compliance with fair housing laws</li> </ul>
<b>Professional relationships</b>	<ul style="list-style-type: none"> <li>no disparagement of competitors; no unfair advantage; respect for others; arbitration of disputes</li> </ul>
<b>Residential property condition disclosure</b>	<ul style="list-style-type: none"> <li>where required, re-seller of residential property must complete and deliver to buyer on or before offering; failure gives buyer right to rescind prior to closing or occupancy; agents must disclose material facts; buyers must acknowledge receipt</li> </ul>

# 21 Closings

## THE CLOSING EVENT

- The setting**
    - sale contract sets date, location, and who participates
  - The closing process**
    - verify contract fulfillment; exchange consideration and title; pay expenses; sign final documents; arrange for recording the transaction
  - Transfer of title**
    - seller gives evidence of marketability-- title abstract or title insurance commitment; may also need affidavit stating no new encumbrances incurred; seller must remove encumbrances or liens prior to the specified date; if seller is paying off mortgage lien, lender provides a payoff statement
  - Transfer of purchase funds**
    - buyer produces funds and documents needed to complete the transaction
  - Escrow procedures**
    - if closing "in escrow," escrow agent holds and disburses funds and releases documents when escrow conditions have been met
  - Lender closing requirements**
    - common: survey, inspections, hazard insurance, title insurance, certificate of occupancy, reserves for taxes and insurance, private mortgage insurance
  - Broker's role**
    - broker's role ranges from nil to conducting the proceedings to reporting the transaction
- REAL ESTATE SETTLEMENT PROCEDURES ACT**
- for residential property, first or second mortgage, federally-related mortgage, assumption modifying loan terms, lender charging over \$50 for assumption
- Information booklet**
    - lender must provide borrower with CFPB booklet, "Your Home Loan Toolkit"
  - Loan Estimate**
    - lender must provide CFPB's H-24 Loan Estimate of settlement costs
  - Mortgage servicing disclosure**
    - lender must disclose who will be servicing loan
  - Closing Disclosure**
    - lender must use CFPB's H-25 Closing disclosure
  - Disclosures after settlement**
    - loan servicers must provide annual escrow statements to borrowers
  - Limits on escrow accounts**
    - places ceiling on amounts lenders may compel borrowers to place in escrow
  - Referral fees and kickbacks**
    - RESPA prohibits payment of referral fees and kickbacks; business relationships between firms involved in the transaction must be disclosed

## FINANCIAL SETTLEMENT OF THE TRANSACTION

- Settlement process**
  - identify closing costs; determine who pays what; do prorations; assign debits and credits; complete closing statement; disburse funds
- Selling terms and closing costs**
  - price, deposits, downpayment, financing, final expenses to be paid at closing; apportionment of expenses determined by sale contract or custom
- Debits and credits**
  - excess of buyer's debits over credits is amount buyer must produce at closing; excess of seller's credits over debits is amount seller must receive
- Non-prorated items**
  - incurred by one party only; not shared
- Prorated items**
  - incurred by buyer or seller in advance or arrears; shared by buyer and seller; typical: real estate taxes, insurance premiums, mortgage interest, rents

## **COMPUTING**

### **PRORATIONS**

#### **12-month/30-day method**

- sale contract or local custom establishes methods of proration to be used for particular items
- determines average daily amount based on 12-month year and 30-day month

#### **365-day method**

- determines an amount using the actual number of calendar days

## **TAXES DUE AT CLOSING**

### **State taxes on deed**

- state, counties and municipalities may impose taxes on transfer

### **State taxes on mortgage**

- state may impose taxes on mortgages, notes and contracts

## **TILA/RESPA INTEGRATED DISCLOSURES RULE**

### **Forms and procedures**

- effective October 3, 2015
- mandatory: Your Home Loan Toolkit booklet at loan application; Loan Estimate form 3 business days after loan application; Closing disclosure 3 business days before consummation

### **Good faith**

- Loan Estimate costs based on best information available
- Closing Disclosure costs equal estimate costs within certain tolerances

### **Types of charges**

- no limitation on increase over estimate
- 10% tolerance charges
- 0 tolerance charges

### **Applicable transactions**

- most closed-end consumer mortgages, including: construction loans, loans secured by vacant land, loans to trusts
- not covered: home equity loans, reverse mortgages, loans on mobile homes, loans by small lenders (no more than 5 loans per year)

### **The H-25 form**

- 5 pages, variable by loan type

## **REPORTING REQUIREMENTS**

### **Who must report**

- "real estate broker" defined by the Tax Reform Act of 1986; buyer's or seller's broker, settlement agent, mortgage lender, other IRS-designated party

### **What must be filed**

- Form 1099-S Information Return
- statements to each party
- tax reporting and withholding if FIRPTA applies (non-resident alien)

# 22

## Real Estate Licensing And Regulation

### STATE LICENSE LAW

- most real estate practitioners must be licensed
- protects public, ensures professional competency of licensees
- establishes: requirements for licensure, guidelines of conduct for maintaining license, commission to administer the law
- applicants need a sound understanding of local license law

### OBTAINING A REAL ESTATE LICENSE

#### Services requiring licensure

- license required to perform a real estate service for another for consideration, specifically: brokerage; property management; appraising; counseling; syndicating; auctioning
- exemptions: wage-paid employees of property owners, transient facility employees, condo or coop managers, cemetery lot merchants, attorneys; court-appointed representatives

#### Types of license

- broker's: individual, corporation, partnership, branch office, non-resident; salesperson's: individual, broker-salesperson
- active if practicing; inactive if not practicing; inactive or expired if renewal requirements not met
- voided: by suspension, revocation, expiration

#### Licensing requirements

- personal: age, mental competence, general education, character
- specific education: completion of required real estate courses
- experience: salesperson experience may be required if applying for a broker's license
- agency affiliation: not necessary
- other: complete application; pass state license examination; complete continuing education if applicable

### LICENSE REGULATION

#### The Real Estate Commission

- state-level government entity that regulates and administers the license law
- oversees licensing process; enforces license law provisions; handles consumer and licensee complaints; consists of appointed commissioners and permanent support staff; maintains education and research foundation

#### Regulation focus

- management of licensing and license status; regulation of real estate schools and programs; regulation of practices of licensees; enactment of professional guidelines to protect public; resolution of disputes and complaints; suspension or revocation of licenses

#### Bonds and recovery funds

- ensure that the public will be able to collect on settlements for damages and money judgments against licensees

# 23

## Risk Management

### **RISK MANAGEMENT STRATEGIES**

- two dimensions of risk: size, probability; risk management: structured approach to uncertainty
- **Avoidance** • refrain from risky activity
- **Reduction** • reduce probability; share responsibility
- **Transference** • pass risk by contract; insurance
- **Retention** • accept risk; self-insurance

### **RISK MANAGEMENT PROCEDURES**

- **Education** • train in laws, forms and procedures, job performance
- **Disclosure** • provide information to reduce misunderstanding & lawsuits; agency, property condition, duties, personal interest
- **Documentation and record keeping** • maintain evidence of compliance; manuals, forms, records, contracts, accounting, other documents
- **Insurance** • general liability, E & O, fire and hazard, flood, casualty, workers, personal property, consequential loss, surety bond

### **PRIMARY AREAS OF RISK**

- **Agency**
  - main failures: to inform and disclose, to fulfill duties
  - disclosures: verbal, written, signed receipt; agency relationship and duties; personal interest in transaction; required information
  - duties: to all– honesty, fairness, care, skill, required disclosures; additional to clients– diligence, loyalty, obedience, confidentiality, accounting, full disclosure
  - conflicts of interest arise from failing to put client’s interest first
  - confidentiality duty lasts forever; laws define what is confidential, how to treat and dispose of information
  - penalties include loss of transaction, compensation, fees and costs, damages, license
- **Property disclosures** • property condition, lead-based paint, other conditions; disclosure may discharge liability; failure to disclose may be construed as misrepresentation
- **Listing and selling process** • areas of risk include listing agreement accuracy, Comparative Market Analysis results, closing cost estimates, advertising, authorizations and permissions, exceeding expertise
- **Contracting process** • contracts for real estate must be in writing; inaccuracy endangers contract; other risks: illegal form, omitted elements, lapsed contingencies, wrong data
  - unauthorized practice of law: non-lawyers may fill in blanks and delete words on standard contract forms; no legal advice to public allowed
- **Fair Housing**
  - advertising may not state preference, limitation or discrimination based on race, color, religion, national origin, sex, handicap, familial status
  - agent must not be involved with discriminatory actions of a client or customer

- Antitrust**
  - government prosecutes cooperative arrangements that raise prices or reduce consumer choices: Sherman Antitrust Act outlaws restraint of trade; Clayton Act outlaws practices that harm competition; Federal Trade Commission Act outlaws unfair methods of competition
  - violations punishable by government criminal and civil actions as well as by private lawsuits; fines, damages, and imprisonment possible
- Rules and regulations**
  - violators of state rules and regulations risk license expiration, revocation, suspension, and other discipline
  - prime causes of discipline include commission of prohibited acts, practicing with an expired license, disclosure failures, earnest money mishandling
- Misrepresentation**
  - unintentional: inaccurate information conveyed unknowingly; subject to fines and license discipline; occurs most often in measurements, property descriptions
  - intentional: fraud, knowingly conveying false information; criminal act subject to fines, license discipline, and incarceration
- Recommending providers**
  - risks include consumer dissatisfaction, possible vicarious liability for illegal acts committed by a recommended provider, undisclosed business relationship (RESPA violation as well as license violation)
  - best practice: do not recommend any vendors, or provide a list of trusted vendors with no recommendation and a disclaimer
- Financing and closing**
  - risk areas include fair housing and ECOA violations; failed transactions because of agent failure to monitor contingency period; failure to ensure proper disclosure of closing costs; RESPA violations
- Trust fund handling**
  - risk areas include mishandling of earnest money deposits; commingling and conversion of trust funds; errors in use of trust accounts



# 24 Property Management

## MANAGEMENT FUNCTIONS

- main manager types: individual broker or firm managing for multiple owners; building manager, employed by owner or other manager to manage a single property; resident manager, employed by owner, broker, or management firm to live and manage on site.
- manager is a fiduciary of the principal; duty to act in principle's best interests; may specialize in a property type
- needed skills: marketing, accounting, finance, construction; financial, physical, administrative services; specific functions determined by management agreement

## Reporting

- monthly, quarterly, or annually; annual operating budget, cash flow reports, profit and loss statements, budget comparison statements

## Budgeting

- operating budget based on expected expenses and revenues; determines rental rates, capital expenditures, reserves, salaries and wages; projects income based on past performance and current market
- potential gross income: total of scheduled rents plus revenues from other sources; effective gross income: total gross minus losses from vacancies, evictions, uncollected rents; net operating income: effective gross minus operating expenses; cash flow: net operating income minus debt service and reserves
- expenses are variable and fixed; capital expenditures are outlays for major renovations and construction; cash reserves set aside for variable expenses

## Renting

- manager must keep property properly rented and tenanted; vacancies managed by rent setting, marketing, tenant relations, good service
- selecting compatible tenants and collecting scheduled rents are top priorities
- legal issues concern compliance with fair housing laws, Americans with Disabilities Act, and ECOA

## Property maintenance

- main consideration: balance between costs of services, owner financial objectives, and tenant needs
- may be routine, preventive, or corrective; staffed in-house or contracted out

## Construction

- tenant alterations, renovations, and expansion; also environmental remediation
- legal concerns: Americans with Disabilities Act; applies to employers with fifteen or more employees; manager to determine feasibility of restructuring, retrofitting, new construction, or other alternatives to comply

## Risk management

- risk ranges from natural disaster to personal injury, terrorism, and employee malfeasance; handled by avoiding or removing the source, installing protective systems, buying insurance, self-insuring (risk retention)
- life safety systems include sprinklers, fire doors, smoke alarms, fire escapes, monitoring systems
- insurance includes casualty, liability, workers' comp, fire and hazard, flood, contents, consequential loss, surety bonds, multi-peril; tenants need their own insurance
- handling of trust funds is a major risk area; mishandling carries heavy penalties

## MANAGEMENT AGREEMENT

- Components**
  - names of parties; property description; lease term; owner's purpose; responsibilities; authority; budget; allocation of costs; reporting; compensation; Equal Opportunity statement
- Rights, duties and liabilities**
  - landlord: receive rent; receive premises in specified condition; enter and inspect; examine books; enter into contracts, hire vendors, set rents; pay management; comply with laws
  - manager: hire and fire; enter into contracts; perform management tasks; maintain records, make reports, budget, collect rent, find tenants, maintain the property, meet owner goals; handle trust funds; comply with laws

## LEASING CONSIDERATIONS

- Lease types**
    - for years, periodic, at will, at sufferance, gross, net, percentage, graduated
  - Owned and leased inclusions**
    - items included or excluded in the lease; owner's insurance covers only what is included; alterations to inclusions only with owner's permission
    - "inclusion" also refers to financial items included as lessee's responsibility, such as operating expenses
  - Reversionary rights of owners**
    - all rights of ownership revert to owner at end of lease term
  - Landlord rights and responsibilities**
    - rights: enter premises, receive payment, retake on termination, pursue remedies; responsibilities: provide habitable conditions; maintain heating, cooling, electrical, plumbing; keep clean and in repair
  - Tenant rights and responsibilities**
    - rights: quiet enjoyment, habitable conditions, right to take action for default; responsibilities: pay rent, obey rules, give proper notice, return property in prescribed condition, use only for intended purpose
  - Evictions**
    - actual: prescribed legal procedure; notice, suit, judgment, taking of premises; constructive: tenant vacates for landlord failure to maintain premises
  - Tenant improvements**
    - ownership of and payment for improvements according to agreement
  - Termination of a lease**
    - causes: expiration, performance, agreement, abandonment, breach, notice, destruction of premises, condemnation, foreclosure, death of either party (tenancy at will), death of landlord (life estate)
  - Security deposit procedures**
    - determined by state law, commission rules, agreement
  - Universal Residential Landlord-Tenant Act**
    - model law regulating lease language and lease terms; adopted by many states
- ## MANAGEMENT BUSINESS
- Sources of business**
    - leasing, asset management, corporate properties, resorts, association management, housing programs, mobile home parks, office buildings; owners, investors, corporations, developers, landlords, condo and homeowners' associations, banks, trusts, syndicates
  - Securing business**
    - develop reputation and competence; obtain training; use effective advertising; make management plan in accordance with owner objectives
  - Professional development**
    - training, designations, certifications to increase and demonstrate competence