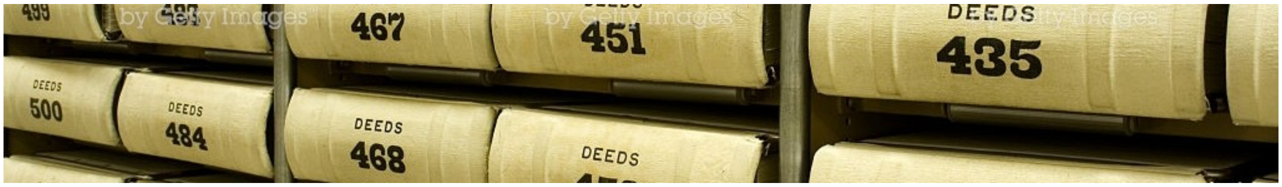
TOPIC 4

Transfer of Title



EXAM TOPICS

TOPIC 4 - Transfer of Title (Salesperson 8%; Broker 7%)

A. Title Insurance

1. What is insured against
2. Title searches, title abstracts, chain of title
3. Marketable vs insurable title
4. Potential title problems and resolution
5. Cloud on title, suit to quiet title *(BROKER ONLY)*

B. Deeds

1. Purpose of deed, when title passes
2. Types of deeds and when used
3. Essential elements of deeds
4. Importance of recording

C. Escrow or closing; tax aspects of transferring title to real property

1. Responsibilities of escrow agent
2. Prorated items
3. Closing statements/TRID disclosures
4. Estimating closing costs
5. Property and income taxes

D. Special processes

1. Foreclosure
2. Short sale

E. Warranties

- Purpose of home or construction warranty programs
- Scope of home or construction warranty programs

A. TITLE INSURANCE

WHAT IS INSURED AGAINST?

1. A policy that protects the insured against monetary losses that result due to a defective title, protection; may protect against:

A. Unrecorded instruments.
B. Forged instruments and deeds.
C. Any information that the examining attorney might overlook.
D. Undisclosed or missing heirs, etc.

2. Remember, title insurance policy does not insure the property. The owner needs to get a homeowners policy or other Insurance as needed.

3. The best Title Policy is one that is issued ―without standard exceptions‖.

4. TYPES OF TITLE POLICIES (BOTH the buyer and the seller must obtain title insurance)

B. OWNER'S POLICY: Usually provided and paid for by the seller (premium is paid once upon purchasing the policy at closing). The policy is issued in the amount of the purchase price and protects the purchaser and his/her heirs against losses due to title defects.

C. LENDER'S (MORTGAGEE'S) POLICY: Insures the lender's interest in the property against losses due to a defective title. Issued in the amount of the mortgage loan. Coverage is reduced with the decrease in mortgage balance. Provided by the borrower for the benefit of the lender (premium is paid once upon purchasing the policy at closing).

TITLE SEARCHES, TITLE ABSTRACTS, CHAIN OF TITLE

TITLE is searched by inspecting the chain of recorded instruments: including deeds, land contracts, assignments, mortgages, etc. The main purpose of the search is getting information about Ownership and Encumbrances.

ENCUMBRANCES: Liens, mortgages, taxes, leases, easements, judgments, deed restrictions, possibly encroachments, etc. attached to property that may become a burden and which may diminish its value. Encumbrances ―run with the land‖, i.e. unless cleared before the sale, it continues to affect the property and must be honored by the new owner.

EVIDENCE OF TITLE: Shown by collecting group of facts resulting from the recording of instruments.

A. CONSTRUCTIVE NOTICE: Public notice, results from recording an instrument.

1. An instrument does not have to be recorded to be valid.
2. A recorded instrument will have a direct effect on title search.
3. Unrecorded instruments do not give the public any notice and have no effect on subsequent owners or lenders who record their interest in good faith.
4. Instruments are recorded CHRONOLOGICALLY, i.e., in the order and date that it was received.

B. ACTUAL NOTICE: Notice given to a person when he actually sees or is notified of an instrument, he may see a person in possession, or notices an encroachment on the property.

Example: A person buying land who sees evidence of a road that passes through the land must take notice although the public record and/or surveys do not mention that road.

PRIORITIES OF LIENS: An instrument that was recorded before another has priority over the latter.

Example: Two mortgage loans are recorded at different times. The first mortgage was recorded in 2010 and the second in 2016. The mortgage that was recorded in 2010 is a first mortgage (senior mortgage lien) and the 2016 mortgage is second (junior mortgage lien). The first mortgage will have priority over the second mortgage in the event of foreclosure and will be paid first when property is sold at a foreclosure auction.

Example: A mortgage is placed on property in the year 2010 but it was not recorded. In 2016 another mortgage was placed on the same property and it was promptly recorded. The latter mortgage created a first (senior) lien because it was recorded first, i.e. before the 2010 mortgage. In the event of foreclosure, the latter mortgage will have priority over the 2010 mortgage and any proceeds resulting from a foreclosure auction will first be directed to it. The 2010 mortgage will not be paid unless there is extra money left from the foreclosure sale.

Generally the priority of specific liens are:

- **Real Estate Taxes (Property Taxes)** (City government imposed)
- **Special Purpose Taxes** (City government imposed)
- **Mortgage Loan Liens (Primary and Junior)**
- **Mechanics & Vendor Lients**
  (In order of first started work date and then filing date)

SUBORDINATION CLAUSE: States that the rights of a mortgage holder will be secondary or subordinate to a later lien or encumbrance, giving the second encumbrance first priority.

CHAIN OF TITLE: The chronological succession of all recorded conveyances that lead to the present title being held. For example: from Jones to Davis to Smith to Nelson and so on

TITLE ABSTRACTS

- A summary of all recorded encumbrances and conveyances affecting title. It does not guarantee title to anybody. An attorney's opinion (**CERTIFICATE OF TITLE**) is required to show that title is marketable.

- Use has mostly ceased in the real estate market in favor of title insurance.

- In Connecticut title is generally considered marketable if there appears to be no unresolved clouds or gaps on the title for the past 40 years and there is no one presently in hostile possession.

CLOUD ON TITLE, SUIT TO QUIET TITLE (BROKER ONLY)

CLOUD ON THE TITLE: Defects affecting marketability of title. Normally title insurance company would attempt to clarify before agreeing to insure title.

Example: Johnson buys property from Sharon and Bill Smith. Bill Smith brings a lady to the closing who claims to be Sharon Smith and who actually presents a fake ID. Later it is discovered that the real Sharon Smith never signed the deed, creating a cloud on the title.

QUIETING TITLE SUIT: Court-ordered hearing held to determine land ownership. Action may be the result of a person's claim to establish ownership and/or remove a cloud from the title.

LIS - PENDENS: A legal document that gives notice of a lawsuit affecting property.

SELLER'S AFFIDAVIT: Seller is required by title insurance company to sign a statement at closing to state certain facts or to declare that he is not aware of any clouds on the title that were not revealed during title search.

SUBROGATION CLAUSE: A clause in the title policy that allows the insurance company who pays a claim to seek reimbursement from the party who caused the loss.

MARKETABLE TITLE: Free from any clouds or defects. Enables a purchaser to resell property without additional effort to clear title.

UNMARKETABLE TITLE: Title may have certain defects that must be cleared. A cloud on the title may be as simple as an unpaid tax bill and as serious as a deed that is missing a signature of one of the owners.

B. DEEDS

PURPOSE OF DEED, WHEN TITLE PASSES

DEED: An instrument used to transfer title to real estate. GRANTOR: One who transfer title to real estate, usually a seller. GRANTEE: The person receiving title, usually a buyer.

DEED ESSENTIALS

A. NAMES AND ADDRESSES of the Grantor and the Grantee.

B. CLAUSE OF CONVEYANCE, (GRANTING CLAUSE): Deed must spell out that title is being transferred from the Grantor to the Grantee.

> **For example:** From Davis to Nelson.

C. TO HAVE AND TO HOLD CLAUSE, (HABENDUM CLAUSE): Specifies how title is conveyed, whether a fee simple absolute, defeasible fee, or life estate.

> **For example:** From Tom to Sharon for her natural lifetime only. Upon her death, title reverts to Tom.

D. VALUABLE CONSIDERATION: A clause acknowledging that the grantor has received consideration, there is no minimum amount of money required by law.

E. LEGAL CAPACITY: Although a grantee can be a minor, a grantor must be of legal age. Property titled to a minor can be deeded by a court-authorized legal guardian.

F. LEGAL DESCRIPTION

G. EXECUTION: Signed by the Grantor: The Grantee does not sign the deed

H. DELIVERY AND ACCEPTANCE: In order for title to pass, the deed must be voluntarily delivered by grantor, and accepted by grantee.

I. RECORDING: Although not mandatory to validate a deed, a deed should be immediately recorded at the register of deeds for public record. To record in Michigan, the following is required by the Register of Deeds in addition to the previous requirements:

1. **Date**
2. **Name and address** of person preparing the deed.
3. **Signatures** appearing on the deed must have names printed or typed nderneath.
4. **Address of the Grantor** and Grantee.
5. **Acknowledgment (notarizing):** Grantor signs in the presence of a Notary Public, a judge, or other official.

An acknowledgment: A declaration made in the presence of an authorized official, by someone stating that s/he is that person and is acting under no pressure and with free will.

TYPES OF DEEDS (GENERAL WARRANTY, SPECIAL WARRANTY, QUITCLAIM) AND WHEN USED

I. WARRANTY DEED

1. GENERAL (FULL) WARRANTY DEED: Contains ALL deed covenants, gives assurance of the quality of title and provides the most liability for title defects against the grantor.

A. COVENANT OF SEISIN: Grantor guarantees that he is "seized" or actually possesses a fee-simple or other interest and s/he has the right to convey such to Grantee.
B. COVENANT AGAINST ENCUMBRANCES: Grantor guarantees that title is free of all encumbrances except those stated in the deed or on the public record and that s/he will protect the buyer's title against any liens, debts, or other encumbrances that may arise.
C. COVENANT OF QUIET ENJOYMENT: Grantor covenants that the property is free from claims of others claiming title to it.
D. COVENANT OF WARRANTY OF TITLE (warranty forever): Grantor forever warrants title to the premises conveyed and promises to defend the Grantee's title against all claims and will compensate the Grantee with money if the title became defective.

E. COVENANT OF FURTHER ASSURANCE: If a cloud (defect) surfaces on title after conveyance, Grantor agrees that s/he will execute any instruments necessary to eliminate the problem.

2. SPECIAL WARRANTY DEED: Conveys title but covenants only against claims arising out of the Grantor's period of ownership. This deed is often used by lenders who sell foreclosed property and provide assurance against title defects for the period of time that the lender (grantor) owned the property, which may be for a short period of time.

3. BARGAIN AND SALE DEED: A bargain and sale deed is in United States real property law, a deed "conveying real property without covenants".
This is a deed "for which the grantor implies to have or have had an interest in the property but offers no warranties of title to the grantee. A bargain and sale deed is especially used by local governments, fiduciaries such as executors, and in foreclosure sales by sheriffs

and referees. The fact that it comes without any warranties from the government means that the new owner may not have good title.

4. QUIT CLAIM DEED: Used to relinquish or quit whatever interest the Grantor may have in the property if any at all. It does not guarantee that Grantor owns the property and gives no assurance to the quality of the title. This deed provides the least liability for title defects against the grantor, yet it places maximum liability against the grantee who is not receiving any covenants of title.

5. JUDICIAL DEED: Ordered by court such as:

1. Executor's Deed: Issued with approval of Probate Court by the —Personal Representative‖ of the estate (executor) named by a person who died —Testate‖, i.e. died leaving a will.

Devise: Real Estate that is willed.
To Devise: To will property to a person or entity.
Devisor: The deceased also referred to as the "testator"
Devisee: The heir.

2. Administrator's Deed: Issued with approval of Probate Court by —Personal Representative‖ of the estate (administrator) who is appointed by probate court because the deceased did not leave a will, i.e. died Intestate.
3. Guardian's Deed: Issued by someone appointed to protect a minor, an insane, or an incapacitated person
4. Trustee's Deed
5. Sheriff's Deed

BILL OF SALE: Transfers title to Chattel (personalty / /personal property). For example, when closing a transaction that involves appliances, a deed would not be suitable to transfer title to a stove or refrigerator. A bill of sale would be needed.
DEED: Transfers real property

C. ESCROW OR CLOSING; TAX ASPECTS OF TRANSFERRING TITLE TO REAL PROPERTY RESPONSIBILITIES OF ESCROW AGENT

1. Verify identity of parties.
2. Parties to sign all necessary documents.
3. Funds and documents to be distributed to the right individuals.
4. Documents are recorded at —Register of Deeds‖.
5. Proper IRS and state forms to be filed such as: 1099-S, Property transfer affidavit.

PRORATED ITEMS

1. Necessary upon sale of property.
2. Property taxes are usually paid annually and a proration is required to provide debits an d credits to both Buyer and seller.
3. For income producing properties, rent received by seller in advance is prorated until end of rental period and paid to buyer at closing.

CLOSING STATEMENTS/TRID DISCLOSURES

A. A broker must shall furnish a closing statement showing all receipts and disbursements affecting buyer and seller. This requirement does not apply if the closing is conducted by a title insurance company.
B. Broker must supervise all closings by being present in person or near a telephone or other telecommunication device to answer any concerns during from closing.
C. Further discussion under the Michigan Rules and Regulations section.
D. Also see the Integrated Disclosure Rules discussed earlier in the "Financing" section under RESPA and TILA.

ESTIMATING CLOSING COSTS

Some of the common debits and credits that are encountered at closing:

Subject	Seller		Buyer	
	Debit	Credit	Debit	Credit
Purchase Price		X	X	
Buyer's Loan				X
Loan Charges/Points			X	
Seller Concessions	X			X
Title Insurance/Owner's	X			
Title Insurance /Lender's			X	
Mortgage Pay-Off	X			
Commission	X			
Delinquent Prop. Tax	X			
Transfer Tax	X			
Outstanding liens	X			
Closing fees (depends on agreement)				

PROPERTY AND INCOME TAXES INCOME TAX IMPLICATIONS OF HOME OWNERSHIP

1. **CAPITAL GAINS:** Result from the sale of a capital asset such as real estate.
2. **BASIS:** Amount of investment owner has in property including purchase price plus improvements.

Example: House purchased for $140,000 and homeowner added a family room for $50,000 and installed new roof for $10,000. The new basis is $200,000, so if house is sold for $235,000, the capital gains will be the following:

$140,000 + $50,000 + $10,000 = $200,000 property adjusted basis
$235,000 – $200,000 = $35,000 capital gain

3. CAPITAL GAINS ON THE SALE OF A HOME:

A. **Gains on the sale of a - principal residencell** are exempt (up to $250,000 per person and $500,000 for a married couple filing jointly)

B. **To qualify as - principal residencell** the taxpayer must have lived in the home for a total of 24 months out of the last 60 months that preceded the sale of the home.

4. **INTEREST DEDUCTIONS:** The IRS allows homeowners an itemized interest deduction on interest paid to finance a principal residence as well as a second vacation home.

Example: if a person who is one that 30% tax bracket is allowed to deduct $5000 on her income tax filing, that person will pay $1500 less in income tax.

NOTE: Real estate taxes on a principal residence will count on an itemized tax return, but not homeowner‘s insurance or condominium association fees.

INCOME TAX IMPLICATIONS FOR REAL ESTATE INVESTMENTS

1. **INCOME TAX** is due on profits generated from investment rental operation.
2. **CAPITAL GAIN TAXES:** Taxes due on gains recognized on the sale of a capital asset such as real estate.
3. **TAX SHELTER - DEPRECIATION** (BROKER ONLY)
A paper loss allowed that decreases yearly profits generated from use of rental or business property.

A. **Land is not depreciable.**

B. **Improvements are depreciable** over a period of time allowing for reduction in taxable income.

Example 1: Residential income property purchased for $350,000 including land valued at $75,000 value. $275,000 improvement is depreciated over 27.5 years at an average of $10,000/yr. If profit from rental operation in one year was $14,000, then $10,000 depreciation is deducted and taxable income is only $4,000.

Example 2: Commercial property $568,000 (including land valued at $100,000). Based on a 39 year depreciation schedule the building depreciates $468,000 ÷ 39 = $12,000 each year. The investor keeps the building for 10 years claiming total depreciation of $12,000 X 10 = $120,000.

Advantages to investing in real estate

1- Tax shelter: Being able to defer a portion (or all) of the profits that are generated by real estate investments.
2- Leverage: Obtaining financing to purchase investment property.
3- Appreciation: Real estate values benefit from inflation as well as supply and demand.
4- Cash flow: Money generated from income-producing properties.

Disadvantages of real estate investments

1- **Liquidity:** Harder to convert to cash in comparison to other investments such as stocks.
2- **Management responsibilities;** those can be alleviate by hiring professional management.
3- Possible loss of value with bad economy.

D. **SPECIAL PROCESS**: Foreclosure & Short Sale – See —Financing‖ section

E. **WARRANTIES**

PURPOSE OF HOME OR CONSTRUCTION WARRANTY PROGRAMS

Home/Construction Warranty

1**-** **A home warranty** (for an existing home or newly built) compensates the buyer in case of defects or breakdowns occurring on property after purchase.
2- **Protects both seller and buyer** since it reduces chances of legal claims against seller and provides buyer with vehicle to recover for damages.
3 – **Protects against anything inside** the unit such as a bad furnace or leaky water heater.

ADDITIONAL TRANSFER OF TITLE STUDY NOTES DETAIL:

I. Title - the right to and evidence of the ownership

II. Voluntary Alienation - the owner intentionally conveys the ownership using some form of deed; may be a gift or a sale. The owner is the grantor. The person receiving title is the grantee.

A. Requirements for a valid deed

1. A grantor who has legal capacity to sign the deed; a deed signed by minors or individuals declared legally incompetent could be either void or voidable.
2. A grantee named to be readily identified
3. A statement of consideration (consult state's laws for any specific requirements)
4. A granting clause¾the words of conveyance
5. A habendum clause¾the "to have and to hold" clause that defines the ownership taken by the grantee
6. An accurate legal description of the property being conveyed
7. Any exceptions or reservations to the title (for example, easements, deed restrictions, or restrictive covenants)
8. The signature of the grantor, sometimes with a seal or before a notary public or other officer of the court
9. Acknowledgment¾that the signature is genuine and a free and voluntary act (consult state's laws for requirements); usually required for recordation
10. The delivery of the deed to and its acceptance by the grantee

B. **Execution of corporate deeds; varies from state to state**

1. The conveyance of corporate-owned real estate requires a proper resolution by its board of directors or some other authority from its bylaws.
2. The deed must be signed by an authorized corporate officer.

C. **Types of deeds**

1. **General warranty deed**
   a. May contain express written warranties; may state "convey and warrant" or "warrant generally" depending on state law
   b. May contain implied warranties according to state statutes
   c. The basic warranties include the following:
      (1) The covenant of seisin—the owner has full ownership and the legal right to convey the title
      (2) The covenant against encumbrances—the title is free from all liens and encumbrances except those specifically stated
      (3) The covenant of quiet enjoyment—the grantor assumes responsibility for protecting the title against the claims of third parties

(4) The covenant of further assurance—the grantor will furnish whatever is needed to make the title good

(5) The covenant of warranty forever—the grantor is liable for reimbursing the grantee for any title interest lost in the future

d. Grantor defends title against both the grantor and against all those who previously held title.

2. **Special warranty deed**

a. Contains clause "remise, release, alienate, and convey"
b. Warrants only that the title was not encumbered while the grantor held it except as noted in the deed.
c. Any additional warranties must be specifically stated in the deed.
d. May be used by a fiduciary

3. **Bargain and sale deed**

a. May state "grants and releases" or "grants, bargains, and sells" in the document, depending on state law
b. Contains no warranties against encumbrances unless stated
c. Only implies that the grantor holds title and possession

4. **Quitclaim deed**

a. Provides the least protection to the grantee
b. Carries no covenants or warranties whatsoever
c. Transfers only what interest the grantor may have, if any
d. May state "remises, releases, and quitclaims"
e. May be used to transfer a right or interest in real estate, such as an easement
f. Often used to cure a defect in title ("cloud on the title")

5. **Deed of trust** - used by a trustor to convey property to a trustee for the benefit of a beneficiary

6. **Reconveyance deed** - executed by the trustee to return (reconvey) title property held in trust to the trustor

7. **Trustee's deed**

a. Used to convey property out of a trust to anyone other than the trustor
b. Executed by the authority granted to the trustee

8. **Deed executed pursuant to a court order**

a. Usually a statutory deed form used to convey title
b. Includes executor's deeds, administrator's deeds, sheriff's deeds, and others
c. Used to convey title to property transferred by court order or by will
d. The full consideration paid is usually stated on the deed.

D. **Transfer tax stamps**

1. Usually payable when the deed is recorded

2. Paid by the seller, buyer, or split, depending on local custom or law

3. Collected by some states, counties, or cities

4. Rates vary from one jurisdiction to another.

5. Some jurisdictions use a transfer declaration form, transfer statement, or affidavit of real property value as basis for calculating tax.

6. Some deeds are exempted from the tax, such as the following:

   a. Gifts
   b. Deeds not made in connection with a sale
   c. Conveyances to or between government bodies
   d. Deeds by charitable, religious, or educational institutions
   e. Deeds securing debts or releasing property as security for a debt
   f. Partitions
   g. Tax deeds
   h. Deeds pursuant to mergers of corporations
   i. Deeds from subsidiary to parent corporations for cancellation of stock

III. Involuntary Alienation - transfers without the owner's consent

A. Transfer by operation of law

1. Eminent domain (through condemnation)
2. Escheat
3. Any type of foreclosure; for example, delinquent real estate taxes or special assessments, mortgage, or deed of trust laws

B. Transfer by natural forces—such as earthquakes, hurricanes, sinkholes, and mudslides

C. Transfer by adverse possession

1. Possession by the trespasser must be open, notorious, continuous for a statutory number of years, and hostile.
2. Tacking permits combining successive periods of adverse possession by different persons.
3. Each jurisdiction has its own minimum requirements before an adverse possession claim can be filed.

IV. Conveyance of a Deceased Person's Property

A. Transfer of title by will¾a devise; the person dies testate

1. A will is a testamentary instrument that becomes effective only after the death of its maker.

2. It must strictly adhere to the laws of the state.
3. It cannot supersede dower and curtesy laws (where they apply)
4. Requirements for a valid will
    a. The maker (the testator) must be of legal age.
    b. The testator must be of sound mind.
    c. It must be a free and voluntary act; the maker must be under no undue influence.
    d. The signing of the will must be witnessed by two or more persons in most states
5. A codicil is a modification of or an amendment to a will.
6. A holographic will is in its maker's own handwriting.
7. A nuncupative will is given verbally by its maker.
8. Some states do not permit property to be conveyed by oral or handwritten wills.

B. Transfer of title by descent¾the laws of the state determine to whom ownership passes; the person dies intestate (see Figure 7.4)
1. The laws of intestate succession vary from state to state.
2. Generally, there are primary heirs (spouse, children).
3. The closeness of one's relationship to the deceased determines the amount of the estate that will be received.

C. Probate proceedings¾the purpose is to see that assets are distributed properly; affects only those assets that do not otherwise distribute themselves by their title.

1. It is a legal process that completes the following:
    a. Proves or confirms the validity of the will
    b. Determines the precise assets of the deceased person c. Identifies the people to whom the assets are to pass
    d. Takes place in the county where the decedent resided
2. An administrator is appointed if there is no will designating an executor, sometimes referred to as "personal representatives."
3. Legal procedures vary considerably from state to state.
4. The decedent's debts must be satisfied before any property can be disbursed to the devisees or heirs.
5. In Practice: Commissions on properties listed through probate are fixed by the court and paid only after the sale has been approved by the court

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NATIONAL TEST TOPIC #4a
TRANSFER OF TITLE #4a
2020 Practice Classroom Quiz

1. In order to deliver title, the following must happen:
- A. Grantor signs deed, grantee signs deed
- B. Grantor and grantee sign, but deed must be delivered and accepted by grantee
- C. Grantor signs and delivers deed to the grantee
- D. Grantor signs, delivers deed, and deed must be recorded.

2. A general warranty deed must contain:
- A. The covenant against encumbrances
- B. A willing, able and ready seller
- C. Monetary consideration
- D. All covenants of title

3. A type of deed that involves no warranties and conveys whatever interest the grantor may have in property is the:
- A. Special warranty deed
- B. Bargain and sale deed
- C. Covenant deed
- D. Quit claim deed

4. Which of the following is not necessary to validate a deed?
- A. A competent grantor
- B. The granting clause
- C. Valuable consideration
- D. Recording

5. A warranty deed contains covenants as to the quality of:
- A. Construction
- B. Environmental problems
- C. Title
- D. The type of use

6. John deeded property to Charles, who failed to record. Later John deeded property to Susan, who accepted it in good faith and recorded it. Who would have superior rights to this property?
- A. Charles, because he bought it first.
- B. John, because by selling it twice neither sale was valid.
- C. Susan, because she recorded first.
- D. Charles and Susan will split the property

7. When closing a transaction, property taxes that were due but not paid are:
- A. A debit to the buyer and a credit to the seller.
- B. A debit to the seller.
- C. A credit to the buyer.
- D. Normally not prorated

8. **On the closing statement, an amount of property tax paid in advance by the owner for a period extending after the day of the closing is:**

A. A debit to the seller.
B. A credit to the buyer.
C. A debit to the seller but a credit to the buyer.
D. A debit to the buyer but a credit to the seller

9**. To inspect for clouds on the title, you must:**

A. Order a survey.
B. Order an environmental audit.
C. Order title search.
D. Pay a visit to the Register of Deeds office.

10. Title insurance will protect against all but which of the following?

A. A missing heir.
B. Forged signature.
C. nrecorded lien.
D. Fire in the house.

11. To remove a cloud from the title through court proceedings, an individual must:

A. Obtain an abstract of title.
B. Obtain actual notice.
C. File a quieting title suit.
D. Obtain title insurance.

12. A lender's title policy is effective until:

A. A claim is paid.
B. Property is sold.
C. A cloud appears on the title.
D. The loan is paid off.

13. All of the following regarding title search is true except:

A. An abstract is the result of recorded conveyances and encumbrances.
B. An abstract will reveal the last owner of record.
C. An abstract is better than a title policy because it insures against monetary losses resulting from a clouded title.
D. Both abstracts and title insurance are the result of title search.

14. The time allowed for recording an instrument is:

A. 24 hours
B. 72 hours
C. No more than 90 days
D. No time limit

15. Constructive notice is established by:

A. Showing the document to an individual.
B. Recording a document at the Register of Deeds office.
C. Filing a document with the court clerk.
D. Notifying an individual by certified mail after recording.

16. In the real estate business, all but which one of the following documents are usually recorded?

A. Deed
B. Land contract
C. Mortgage
D. Promissory note.

17. Helen has two mortgages on her property. One was placed in 1990 when she bought her home and the other in 1997 when she took a home equity loan from a different lender. It appears that the first lender failed to record the mortgage. Which of the following is true?

A. The first lender has a senior position since they had given the money first and the mortgage they received was dated earlier than the second mortgage.
B. Upon foreclosure, the 1990 mortgage will be paid first, and if any funds are left, then it will go to the second mortgage dated 1997.
C. If the 1997 home equity loan was recorded, then it became a senior lien.
D. Both loans have equal standing in the eye of the law.

18. All of the following must take place at the closing except:

A. Deed is signed by the seller and buyer.
B. Closing statement is provided and signed by the broker.
C. Closing is supervised by the broker.
D. Documents are sent to be recorded at the Register of Deeds office.

19. The clause in the title policy that allows an insurance company who paid a claim to seek reimbursement from the party who caused the loss is called:

A. Subordination clause.
B. The cloud clause.
C. Quieting title clause.
D. Subrogation clause.

20. Which of the following is most likely a disadvantage to real estate ownership?

A. Leverage.
B. Cash flow.
C. Liquidity.
D. Appreciation

21. A Bill of Sale is used:

A. Strictly when furniture is sold with a house.
B. When real estate that houses a business is sold.
C. To transfer title to chattel
D. When subsurface rights like oil and minerals are sold.

22. Which type of deed provides the least liability to the Grantor?

A. General warranty deed
B. Full warranty deed
C. Quit claim deed
D. Special warranty deed

23. **All of the following are considered differences between an owner's title policy and the lender's policy except:**

A. One of them covers the purchase price while the other covers the loan amount.
B. One is paid for by the seller while the other is paid for by the buyer/borrower.
C. One protects the buyer while the other protects the lender.
D. One compensates the buyer for losses due to a defective title while the other guarantees to the lender that title will not be defective.

24. All of the following judicial deeds except:

A. Sherriff's deed
B. Administrator's the
C. Guardian's the
D. Special warranty deed

25. The main purpose of the settlement statement is to:

A. Show seller concessions
B. State the amount of the broker's commission
C. Allow credit for buyer's deposit
D. Describe debits and credits for buyer and seller

26. Helen signs a buyer agency contract with her nephew Tom. The contractual relationship has beeen established with:

A. Tom
B. Tom's broker
C. Potential sellers
D. Brokers in the MLS

ANSWERS – TOPIC 4a: TRANSFER OF TITLE 4a

1. C
2. D
3. D
4. D
5. C
6. C
7. B
8. D
9. C
10. D
11. C
12. D
13. C
14. D
15. B
16. D
17. C
18. A
19. D
20. C
21. C
22. C
23. D
24. D
25. D
26. B

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NATIONAL TEST TOPIC #4b

TRANSFER OF TITLE #4b

2020 Practice Classroom Qui

1. **When real estate is sold under an installment land contract and the buyer takes possession of the property, the legal title**
   A) is subject to a purchase-money mortgage.
   B) must be transferred to a land trust.
   C) is kept by the seller until the purchase price is paid according to the contract.
   D) is transferred to the buyer.

2. **The pledging of property as security for payment of a loan without surrendering possession is**
   A) disintermediation.
   B) equity.
   C) hypothecation.
   D) subordination.

3. **A "friendly foreclosure" enables a mortgagor to prevent the mortgagee from taking the property by statutory means. This can be accomplished by use of a(n)**
   A) deed in lieu of foreclosure.
   B) reconveyance deed.
   C) assumption.
   D) escrow deed.

4. **The mortgagee foreclosed on a property after the borrower defaulted on the loan payments. At the foreclosure sale, however, the house sold for only $129,000. The unpaid balance of the loan at the time of the sale was $140,000. What must the lender do to recover the $11,000 the borrower still owes?**
   A) Sue for damages
   B) Sue for specific performance
   C) Seek a judgment by default
   D) Seek a deficiency judgment

5. **In what way does a deed of trust differ from a mortgage?**
   A) Number of parties involved in the loan
   B) Obligation of the borrower to repay the funds
   C) Redemption rights allowed after foreclosure
   D) Time period permitted to cure a default

6. **When a mortgage loan has been paid in full, it is important for the borrower to be sure that**
   A) the paid note is placed in a safe deposit box.
   B) he or she obtains a deed of partial reconveyance.
   C) the paid mortgage is returned to the lender.
   D) a satisfaction of mortgage is recorded.

7. The clause in a trust deed or mortgage that permits the lender to declare the entire unpaid balance immediately due and payable upon default is the

A) judgment clause.
B) escalator clause.
C) forfeiture clause.
D) acceleration clause.

8. An existing mortgage loan can have its lien priority lowered through the use of a

A) hypothecation agreement.
B) satisfaction of mortgage.
C) subordination agreement.
D) reconveyance of mortgage.

9. The fee charged by a mortgage broker to arrange a loan is a(n)

A) prepayment penalty.
B) advance interest payment.
C) loan origination fee.
D) prepayment of mortgage insurance.

10. A promissory note

A) may not be executed in connection with a real estate loan.
B) is an agreement to perform or not to perform certain acts.
C) makes the borrower personally liable for the debt.
D) is a guarantee by a government agency.

11. A mortgagor is the one who

A) gives a mortgage.
B) holds a mortgage.
C) provides mortgage funds.
D) forecloses on a mortgage.

12. A land contract provides for the

A) sale of unimproved land only.
B) sale of real property under an option agreement.
C) conveyance of legal title at a future date.
D) immediate transfer of reversionary rights.

13. A woman has owned her house for over 50 years. It has fallen into disrepair, but because she lives on a fixed income she does not have the money to make the needed repairs. She has a considerable amount of equity in the house. What type of loan best suits her needs?

A) Home equity loan
B) Reverse mortgage
C) Blanket loan
D) Open-end loan

14. A type of long-term financing that has become popular because initial payments are lower due to no principal being paid is called a(n)
A) amortized loan.
B) balloon loan.
C) package loan.
D) interest-only loan.

15. The type of mortgage loan that uses both real and personal property as security is a
A) blanket loan.
B) package loan.
C) purchase-money mortgage.
D) wraparound loan.

16. Freddie Mac
A) operates mostly in the primary mortgage market.
B) operates mostly in the secondary mortgage market.
C) guarantees payment of Freddie Mac mortgages.
D) buys mostly FHA loans.

17. Which of the following would be considered a trigger item under Regulation Z?
A) “Low monthly payments”
B) “FHA financing available”
C) “A steal at only $175,000!”
D) “Only $10,000 down”

18. PMI is the acronym for private mortgage insurance, which is often used by borrowers whose LTV (loan-to-value ratio) is less than 20 percent. Lenders must cease charging PMI when the LTV reaches
A) 22 percent.
B) 27 percent.
C) 29 percent.
D) 35 percent.

19. When compared with a 30-year payment period, taking out a loan with a 20-year payment period would result in
A) slower equity buildup.
B) greater impound requirements.
C) lower monthly payments.
D) higher monthly payments.

20. An extension of credit from a seller to a buyer to allow the buyer to complete the transaction is called a
A) growing-equity mortgage.
B) purchase-money mortgage.
C) package mortgage.
D) blanket mortgage.

21. Which statement is *TRUE* about VA-guaranteed mortgages?

A) Discount points must be paid by the seller.
B) The borrower may have a prepayment penalty clause in the loan.
C) Funding fee amounts are negotiable.
D) The borrower must apply for a certificate of eligibility.

22. A mortgage broker generally offers which of the following services?

A) Handling the escrow procedures
B) Bringing the borrower and the lender together
C) Providing credit qualification and evaluation reports
D) Granting real estate loans using investor funds

23. Fannie Mae, Ginnie Mae, and Freddie Mac all

A) originate residential mortgage loans.
B) purchase existing mortgage loans.
C) insure residential mortgage loans.
D) guarantee existing mortgage loans.

24. A woman's son will start college soon. She has lived in her home for ten years. What financing option would be preferable for the woman to obtain funds to pay for her son's schooling?

A) Participation financing
B) Open-end loan
C) Wraparound loan
D) Home equity loan

ANSWERS – TOPIC 4b: TRANSFER OF TITLE 4b

1. C
2. C
3. A
4. D
5. A
6. D
7. D
8. C
9. C
10. C
11. A
12. C
13. B
14. D
15. B
16. B
17. D
18. A
19. D
20. B
21. D
22. B
23. B
24. D

GENERAL WARRANTY DOCUMENT FORM (SAMPLE - SPECIMEN)

Prepared By

Name: ______________________________
Address: ____________________________
____
State: _____________ Zip Code: ________

After Recording Return To

Name: ______________________________
Address: ____________________________
____
State: _____________ Zip Code: ________

Space Above This Line for Recorder's Use

CONNECTICUT GENERAL WARRANTY DEED

STATE OF CONNECTICUT

____________________ COUNTY

KNOW ALL MEN BY THESE PRESENTS, That for and in consideration of the sum of ___________________________ ($__________________) in hand paid to _____________________, a _________________, residing at ___________________, County of ___________, City of _______________, State of _______________ (hereinafter known as the "Grantor(s)") hereby grants to _____________________, a _________________, residing at ___________________, County of ___________, City of _______________, State of _______________ (hereinafter known as the "Grantee(s)") with warranty covenants to the title, interest, and claim in or to the following *described real estate (*and in Exhibit A if attached), situated in ____________________ County, Connecticut to-wit:

____

____

____

[INSERT LEGAL DESCRIPTION HERE AND/OR ATTACH EXHIBIT A]

TOGETHER WITH all the rights, members and appurtenances to the Real Estate in anywise appertaining or belonging thereto.

Page 1 of 3

TO HAVE AND TO HOLD, the tract or parcel of land above described together with all and singular the rights, privileges, tenements, appurtenances, and improvements unto the said Grantees, their heirs and assigns forever.

And said Grantors, for said Grantors, their heirs, successors, executors and administrators, covenants with Grantees, and with their heirs and assigns, that Grantors are lawfully seized in fee simple of the said Real Estate; that said Real Estate is free and clear from all Liens and Encumbrances, except as hereinabove set forth, and except for taxes due for the current and subsequent years, and except for any Restrictions pertaining to the Real Estate of record in the Probate Office of said County; and that Grantors will, and their heirs, executors and administrators shall, warrant and defend the same to said Grantees, and their heirs and assigns, forever against the lawful claims of all persons.

IN WITNESS WHEREOF, Grantor has executed and delivered this General Warranty Deed under seal as of the day and year first above written.

______________________________	______________________________
Grantor's Signature	Grantor's Signature
______________________________	______________________________
Grantor's Name	Grantor's Name
______________________________	______________________________
Address	Address
______________________________	______________________________
City, State & Zip	City, State & Zip

In Witness Whereof,

______________________________	______________________________
Witness's Signature	Witness's Signature
______________________________	______________________________
Witness's Name	Witness's Name
______________________________	______________________________
Address	Address
______________________________	______________________________
City, State & Zip	City, State & Zip

STATE OF CONNECTICUT)

COUNTY OF ___________________)

I, the undersigned, a Notary Public in and for said County, in said State, hereby certify that ______________________________ whose names are signed to the foregoing instrument, and who is known to me, acknowledged before me on this day that, being informed of the contents of the instrument, they, executed the same voluntarily on the day the same bears date.

Given under my hand this ____ day of ____________________, 20___.

____

Notary Public

My Commission Expires: ______________

END

TOPIC 5

Mandated Disclosures

EXAM TOPICS

TOPIC 5 - Property disclosures (Salesperson 6%; Broker 7%)

A. Property condition

1. Property condition that may warrant inspections and surveys
2. Proposed uses or changes in uses that should trigger inquiry about public or private land use controls

B. Environmental issues requiring disclosure

C. Government disclosure requirements (LEAD)

D. Material facts and defect disclosure

STUDY NOTES:

PROPERTY CONDITION & DISCLOSURE

PROPERTY OWNER'S ROLE REGARDING RESIDENTIAL PROPERTY CONDITION DISCLOSURE REPORT (PDR) STATEMENT:

- Sellers of residential property (one to four family dwellings) must complete and sign the **Residential Property Condition Disclosure Report (PDR)** and deliver it to the buyer when entering into a binding purchase agreement.
- If purchaser signs an offer without being provided with disclosure, s/he may withdraw from transaction before closing and receive deposit refund.
- Real estate offices (or the real estate licensee) must make the form available to the public even if the person requesting the form is not a client of the agent.
- Purchase agreement must identify that the buyer has or has not received the (PDR).
- See the Residential Property Condition Disclosure Report at the end of this section.

SELLER'S RESPONSIBILITY FOR WITHOLDING INFORMATION

FRAUD: An intentional mis-statement of facts.

> **Example:** Seller knows that property is situated on 2 acres but he states that he has 5 acres.

SILENT FRAUD (Non-Disclosure): The act of withholding information regarding concealed property defects from the buyer while the seller knows if such information is disclosed, it may result in losing the sale or offering a lower price.

> **Example:** Seller paves over an old, leaky underground storage tank because he does not want a potential buyer to find out about it.

MISREPRESENTATION (INNOCENT MISREPRESENTATION): An innocent misstatement of facts.

> **Example:** Seller believes that his property is situated on 5 acres and that is what he documents in the sale, but the truth is that the property only sits on 2 acres.

LATENT DEFECT: A defect that is hidden but known to the seller only and cannot be revealed by an ordinary inspection of the agent or buyer, such as a crack in a basement wall that is concealed behind some drywall or paneling. A "***non-disclosure***" of a defect will result in seller committing "***silent fraud***".

PATENT DEFECT: A defect that can be discovered as a result of a reasonable inspection that is conducted on the property, such as an obvious roof leak, furnace problem, etc.

LICENSEE'S ROLE REGARDING PROPERTY CONDITION

1- If licensee is aware of certain property defects, licensee has a duty to disclose the information to the buyer even if licensee was a seller's agent.

2- Licensee must encourage the seller to disclose all known defects even if the defect is not addressed in the seller's disclosure statement.

STATE POSITION REGARDING DISCLOSURE: A licensee's disclosure of material facts in the property shall not be considered grounds for disciplinary action by the DCP/REC against the licensee, despite a claim by the seller that such disclosure constituted disloyalty to the seller.

MATERIAL FACTS RELATED TO PROPERTY CONDITION OR LOCATION

MATERIAL FACTS: Have direct effect on value such as a leak in the roof, pollution, a bad furnace, etc. It may not be a defect but an issue that a buyer must know such as the fact that the seller has made an addition to the property without a permit or has an ongoing legal problem with a neighbor or the association. Material facts must be disclosed to the buyer.

NON-MATERIAL FACTS: Have no effect on value such as the reason for the sale, seller is sick, getting a divorce, seller lost job and is desperate for money, or, for example, that a murder or suicide has occurred in the house. No duty is imposed to disclose. In fact, as agent of seller, you will jeopardize seller's bargaining position by voluntarily disclosing such unnecessary information.

ENVIRONMENTAL ISSUES REQUIRING DISCLOSURE LEAD PAINT DISCLOSURES

1- As discussed earlier under the section "***land use controls and regulations***", a property may have certain environmental hazards that must be dealt with when selling or leasing that property.

2- Environmental hazards may also exist outside the property such as a nearby dump, air pollution a nearby factory, oil refinery, Storage tanks that are buried outside the property, and so on.

3- The seller's disclosure statement addresses certain issues but the fact remains that if the seller or agent knows of any hazards, full disclosure is required. Keep in mind that the seller's disclosure statement only applies to residential property (1-4 family dwellings), not that a seller of commercial property or vacant land could not voluntarily use it, but remains unlikely that it will be used in other than residential sales.

AGENCY DISCLOSURE

A. **Disclosure of the agency relationship is required in Connecticut;** it is required at the first meaningful contact with a buyer or seller.
B. **Dual agency is not allowed unless all parties agree to it;** however, dual agency is illegal in some states. The disclosure should be made before the individual discloses any confidential information to the broker.

PROPERTY DISCLOSURE

A. **Latent defects**—a hidden structural defect that would not be discovered by ordinary inspection, such as a part of the property being built partly on an adjoining property or a zoning violation.
   1. Seller has duty to discover and disclose any known latent defects that threaten personal safety or structural soundness.
   2. Buyers have been able to receive damages or terminate the offer to purchase in a case where a seller did not reveal known latent defects.
   3. Some states require a seller of residential property to provide a property condition report for all prospective buyers.
   4. Some states also require the licensee to discover and disclose to prospective buyers any material facts that may affect the property's desirability or value in spite of the seller's lack of knowledge or failure to disclose.

ENVIRONMENTAL DISCLOSURES

1. A real estate broker should be able to notice potential environmental hazards in a property that would be readily apparent to a real estate broker and urge that the buyer or seller have the potential hazard evaluated by a qualified third party.
2. Broker should be aware of the **Comprehensive Environmental Response Compensation and Liability Act (CERCLA)** of 1980 which was amended as the **Superfund Amendment and Reauthorization Act (SARA)** of 1986.
   a. **Established fund of $9 billion called Superfund** to clean up uncontrolled hazardous waste dumps and respond to spills.
   b. **Created a process of identifying liable parties and ordering them to take responsibility for the cleanup.**
   c. **Liability under Superfund isconsidered to be strict, joint and several, and retroactive**
      (1) **Strict liability**—owner is responsible to the injured party without excuse.
      (2) **Joint and several liability**—each individual owner is personally

responsible for the damages in whole; if only one owner is financially able to handle the total damage, then that owner will have to pay all and attempt to collect the proportionate share of the rest of the owners from them.

(3) **Retroactive liability**—liability for actions before CERCLA was passed. For example, in the Love Canal case all the waste was dumped long before CERCLA was passed in 1980, but the release of that waste was current and causing injury after the statute was enacted. Retroactive liability means that parties found responsible for causing a release are liable even if their actions occurred prior to CERCLA's enactment.

d. **In 2001–2002 the Brownfields Revitalization and Environmental Restoration Act** and subsequent Small Business Liability Relief and Brownfields Revitalization Act were enacted to further reduce the risk of innocent landowners who purchased once environmentally contaminated real estate. This legislation helped to rejuvenate many deserted, defunct, and derelict toxic industrial sites by diminishing the innocent landowner's liability exposure and providing them with the opportunity to expense cleanup costs rather than capitalize them.

C. Brokers should be familiar with environmental hazards known to be common to their market area.

D. The listing broker and selling broker, if a subagent, must inform the seller or lessor of their obligations for environmental disclosures under **the Residential Lead-Based Paint Hazard Reduction Act of 1992 for dwellings built prior to 1978:**

1. Homebuyers must be alerted to any lead-based paint or related hazards.
2. Homebuyers must be given an agreed-upon time period for the opportunity to conduct a lead-based paint inspection or risk assessment at their expense.
3. A Certification and Acknowledgment of Disclosures must be attached to the offer to purchase.
4. A copy of the Certification and Acknowledgment must be kept by the seller and both agents for three years after closing or the beginning of the lease.

MATERIAL FACTS FOR SELLER'S AGENT INCLUDE

1. **disclosure of all offers**,
2. **buyer's ability to offer a higher price** (in most states),
3. **disclosing names of prospective buyers** as well as any relationship, such as buyer being related to licensee, and
4. **disclosure of known material defects** in property.

MATERIAL FACTS FOR BUYER'S AGENT INCLUDE

1. **disclosing property deficiencies**,
2. **disclosing provisions of offer** to purchase that are not favorable to the buyer,
3. **recommending the lowest price** the buyer should offer regardless of the list price, &
4. **disclosing how long** the property has been listed.

NATIONAL TEST TOPIC #5a

MANDATED DISCLOSURES #5a

2020 Practice Classroom Quiz

1- The purpose of the seller's disclosure statement is to:

A. Determine all defects with the property
B. Inform a potential buyer of conditions known to the seller
C. Be able to sue the seller for any defects with the property
D. Stop the buyer from withdrawing from the sale before closing

2- A buyer signed a purchase agreement and was later able to legally withdraw from the transaction and received a refund of the deposit. Under which of the following circumstances was the buyer able to rescind the transaction?

A. The buyer could not be approved for a loan at favorable interest rates
B. The buyer was surprised that his employer was transferring him to another city
C. The buyer heard that someone was killed in the house
D. The buyer did not receive a seller's disclosure statement

3- All of the following are material facts except:

A. Leak in the roof
B. Crack in the basement wall
C. Problem with plumbing
D. Seller is anxious to sell

4- Seller's disclosure statement must be provided to buyer:

A. No later than nine business days after signing the offer to purchase
B. Before an offer to purchase is signed
C. Any time before closing
D. No later than two days after closing

5- The listing salesperson has no duty to inform a buyer that:
A. Zoning is a problem for the property
B. Leaks from a nearby toxic waste dump site have caused underground pollution.
C. Seller indicated that she will accept less for the property
D. The city inspector will probably not issue a permit to build on this property unless a cleanup takes place

6- An owner asks the salesperson if his company will accept less commission. The salesperson must:

A. Leave the commission blank after signing the listing agreement and see if the broker will later allow a lower commission.
B. Tell the owner that all commissions are set by the state and there is nothing he can do
C. Lower the commission to any reasonable amount agreed upon between the salesperson and the owner.
D. Tell the owner that the decision must be made by the broker and he has no authority to accept less commission.

7- The street in your neighborhood has been paved by the city. How will that affect your tax bill?

A. Millage rate will increase.
B. Assessed value will decrease.
C. You may receive a bill for special assessments
D. Your property tax will be lowered.

8- An agent inspects a new listing and notices obvious leaks in the roof as well as around windows. He is told by the seller that the furnace is not working properly and that all the defects will be disclosed on the seller's disclosure statement. The agent also notices water in the basement, but the seller tells him to ignore the water because he had paid a company to fix it but it still leaked, therefore they were coming back to fix it again under warranty. Which of the following is NOT considered to be proper behavior by agent?

A. Make sure that the leaks and the furnace issue are disclosed
B. Recommend an inspection to a potential buyer just in case there are more defects in the property
C. Since the issue with the basement is covered by warranty, there is no need to be concerned with it
D. Provide a completed seller's disclosure statement to the buyer before signing the purchase agreement

9- A provision placed in the deed by the seller aimed at controlling the present and future use of property is called:

A. Seller restriction
B. Land use regulation
C. Unnecessary burden on the buyer
D. Deed restriction

10- An agent is selling a vacant lot in a neighborhood that is not served with sanitary sewers. The agent should make the purchase agreement subject to

A. A foundation inspection
B. A percolation test
C. A soil sampling inspection
D. A building permit

11- Which of the following would be covered under a home / construction warranty?

A. Damages resulting from overpaying for the property
B. Damages resulting from a defective title
C. Damages resulting from a defective furnace
D. Damages resulting from an unpaid water bill prior to closi

12- John is thinking about selling his house but wants to try it –by owner‖ to see if he can save the commission. Sally provides John with a free market analysis hoping to list the property and informs him of the necessity of providing a seller's disclosure statement. John thanks Sally for her service but refuses to list the house with her. If John needs a copy of the seller's disclosure form, where can he get it?

A. Sally must provide it to him even though he did not hire her
B. Sally can refer him to the state website where he can download it
C. Sally can suggest that he contact a lawyer or the local government
D. Sally should tell him that the disclosure is required only when a licensee is involved in the sale of the property

END

ANSWERS – **TOPIC 5a: PROPERTY CONDITION & DISCLOSURE**

1. B
2. D
3. D
4. B
5. C
6. D
7. C
8. C
9. D
10. B
11. C
12. A

NATIONAL TEST TOPIC #5b

MANDATED DISCLOSURES #5b

2020 Practice Classroom Quiz

1. Broker Bob is going to contact customer Paula who would like to see one of Bob's listings. Bob should make his agency disclosure

1. prior to meeting with Paula
2. prior to discussing Paula's financial qualification and type of house desired.
3. prior to actually showing the listed property
4. prior to writing an offer to purchase.

2. Which of the following would NOT be classified as a latent defect?

1. An unknown underground oil tank
2. Hidden structural damage
3. A large crack in the living room ceiling
4. A cracked heat exchanger in the furnace

3. Which of the following statements does NOT correctly describe the status of dual agency?

1. Dual agency is legal in all states.
2. Dual agency is not allowed unless all parties agree to it.
3. Disclosure of dual agency should be made when preparing an offer to purchase.
4. Disclosure of dual agency should be made prior to the closing of a real estate transaction.

4. The Comprehensive Environmental Response. Compensation, and Liability Act was amended in 1986 to protect innocent landowners from cleanup liability through which legislative action?

1. SARA
2. FIREEA
3. Title VIII
4. Title X

5. The Residential Lead-Based Paint Hazard Reduction Act of 1992 does NOT require that

1. the seller disclose any lead-based paint or related hazards.
2. homebuyers be given an agreed-upon time period for the opportunity to conduct a lead-based paint inspection or a risk assessment at their own expense.
3. a Certification and Acknowledgment of Disclosure be attached to the offer to purchase.
4. a copy of the Certification and Acknowledgment be kept by only the listing broker.

6. The Residential Lead-Based Paint Hazard Reduction Act of I992 requires that copies of the Certification and Acknowledgment be kept for

I. one year after closing.
2. two years after closing.
3. seven years after closing.
4. five years after closing.

7. Which of the following statements would NOT be a material fact to be disclosed by a seller's agent?

1. The buyer's ability to make a higher offer
2. Disclosure of a roof that leaks
3. Discussion of the advantages of an offer to purchase
4. Knowledge of active infestation of termites

8. Which of the following statements would NOT be a material fact to be disclosed by a buyer's agent?

1. Disclosure of how long the property has been listed
2. Buyer's ability to make a higher offer
3. Recommend the lowest price the buyer should offer regardless of the list price
4. Disclosure of provisions of offer to purchase that are not favorable to buyer

9. Which of the following does NOT correctly describe the status of agency disclosure?

I. Disclosure is required in some states.
2. Disclosure is required at the first meaningful contact with a buyer.
3. Disclosure is required at the first meaningful contact with the seller.
4. Disclosure is required in every state.

10. CERCLA is a law that deals with

1. fair housing legislation.
2. environmental legislation.
3. appraisal legislation.
4. banking legislation.

11. Legislation that has helped resurrect deserted, defunct, and derelict toxic industrial sites is known as

I. DNR.
2. Waste field.
3. Due diligences.
4. Brownfiields legislation.

12. An owner had a grease fire and it spread to the ceiling. The kitchen was remodeled and the charred ceiling joists were sealed with paint. When the seller sells the property, the hidden charred ceiling joists should be disclosed as
1. nothing because they were repaired.
2. discoverable defects.
3. caveat emptor.
4. latent defects.

13. What federal legislation would a community call upon to clean up a toxic waste site?
1. HUD
2. Regulation Z
3. CERCLA
4. Title VIII

14. If a buyer's agent knows that the house her buyer desires to purchase has been stigmatized by a recent murder-suicide, what ethically should the buyer's agent do?
1. Remain silent to protect the seller
2. Remain silent because the incident didn't harm the structure
3. Disclose it to the buyer after the purchase agreement is signed
4. Disclose it to the buyer before the buyer writes an offer

ANSWERS: **TOPIC 5b: Mandated Disclosures QUESTIONS (5b)**

1. (2) While this is generally correct, you should check with your state licensing board on the disclosure timing.

2. (3) A latent defect would not be discovered by an ordinary inspection.

3. (1) Dual agency is not legal in some states. Moreover, dual agency is not allowed in any state unless all parties agree to it.

4. (1) **SARA** (Superfund Amendments and Reauthorization Act) was enacted to create an innocent landowner defense against the strict liability interpretation of CERCLA.

5. (4) A copy of the Certification & Acknowledgment must be kept by the seller and both agents.

6. (3) Copies must also be kept for seven years after the beginning of a lease.

7. (2) Property defects caused by deferred maintenance.

8. (2) A seller's agent would be required to disclose the buyer's ability to make a higher offer unless prohibited by state law.

9. (1) Agency disclosure is required in every state; therefore, the first response is incorrect. Agency disclosure is generally required at the first meaningful contact with either buyer or seller.

10. (2) Environmental legislation that funds federal money for the cleaning up of toxic waste sites; also called the Superfund.

11 (4) Brownfields legislation guidelines give individual states the authority to determine how to clean up defunct and derelict toxic industrial sites.

12. (4) Latent defects are hidden structural defects that can't be discovered by ordinary inspection. These defects can
potentially threaten the soundness or safety of the property. Caveat emptor means "buyer beware," but with seller property disclosure laws that kind of thinking is unfair and unacceptable.

13. (3) CERCLA is also known as the Superfund. HUD enforces fair housing laws; Regulation Z is legislation that requires lender disclosure of cost of credit; & Title VIII is fair housing legislation.

14. (4) The buyer's agent has an ethical duty to tell the buyer everything he or she knows that relates to the decision-making process unless the disclosure violates the law, such as the racial composition of a neighborhood.

PROPERTY CONDITION DISCLOSURE FORM REPORT (SAMPLE SPECIMEN ONLY)

STATE OF CONNECTICUT
DEPARTMENT OF CONSUMER PROTECTION
450 Columbus Blvd, Suite 901 ♦ Hartford, CT 06103

RESIDENTIAL PROPERTY CONDITION DISCLOSURE REPORT

The Uniform Property Condition Disclosure Act (Connecticut General Statutes Section 20-327b) requires the seller of residential property to provide this disclosure to the prospective purchaser prior to the prospective purchaser's execution of any binder, contract to purchase, option, or lease containing a purchase option. These provisions apply to the transfer of residential real property of four dwelling units or less, including cooperatives and condominiums, made with or without the assistance of a licensed broker or salesperson. The seller will be required to credit the purchaser with the sum of $500 at closing if the seller fails to furnish this report (Connecticut General Statutes Section 20-327c).

<u>INSTRUCTIONS TO SELLERS:</u>
1. You **must** answer **all** questions to the best of your knowledge.
2. You are required to identify and disclose any problems regarding the subject property.
3. **Your real estate licensee cannot complete this form on your behalf.**
4. "UNK" means Unknown, "N/A" means Not Applicable.
5. If you need additional space to complete any answer or explanation, attach additional page(s) to this form. Include subject property address, seller's name and the date.

Pursuant to the Uniform Property Condition Disclosure Act, the seller is obligated to answer the following questions and to disclose herein any knowledge of any problem regarding the following:

A. SUBJECT PROPERTY

1) Name of seller(s):____

____

2) Street address, municipality, zip code:________________________________

____

YES	NO	UNK	N/A	**B. GENERAL INFORMATION**
				3) What year was the structure built? ______________________
☐	☐	☐	☐	4) How long have you occupied the property?______________ If not applicable, indicate with N/A.
☐	☐	☐	☐	5) Does anyone else claim to own any part of your property, including, but not limited to, any encroachments? If yes, explain:______________________________________
☐	☐	☐	☐	6) Does anyone other than you have or claim to have any right to use any part of your property, including, but not limited to, any easement or right of way? If yes, explain:________________
☐	☐	☐	☐	7) Is the property in a flood hazard area or an inland wetlands area? If yes, explain:______________

Seller Initials_____ **Buyer Initials**______ Revised 08/2018

PROPERTY CONDITION DISCLOSURE FORM REPORT (SAMPLE PAGE 2 OF 7)

YES	NO	UNK	N/A	B. GENERAL INFORMATION (Continued)
☐	☐	☐	☐	8) Do you have any reason to believe that the municipality in which the subject property is located may impose any assessment for purposes such as sewer installation, sewer improvements, water main installation, water main improvements, sidewalks or other improvements? If yes, explain:____________________
☐	☐	☐	☐	9) Is the property located in a municipally designated village district, municipally designated historic district, or listed on the National Register of Historic Places? If yes, explain: ____________________ **Note**: Information concerning village districts and historic districts may be obtained from the municipality's village district commission, if applicable.
☐	☐	☐	☐	10) Is the property located in a special tax district? If yes, explain:____________________
☐	☐	☐	☐	11) Is the property subject to any type of land use restrictions, other than those contained within the property's chain of title or that are necessary to comply with state laws or municipal zoning? If yes, explain:____________________
☐	☐	☐	☐	12) Is the property located in a common interest community? If yes, is it subject to any community or association dues or fees? Please explain:____________________
☐	☐	☐	☐	13) Do you have any knowledge of prior or pending litigation, government agency or administrative actions, orders or liens on the property related to the release of any hazardous substance? If yes, explain:____________________

YES	NO	UNK	N/A	C. LEASED EQUIPMENT
☐	☐	☐	☐	14) Does the property include any leased or rented equipment that would necessitate or oblige either of the following: the assignment or transfer of the lease or rental agreement(s) to the buyer **or** the replacement or substitution of the equipment by the buyer? If yes, indicate by checking all items that apply:

- ☐ Propane fuel tank
- ☐ Water heater
- ☐ Security alarm system
- ☐ Fire alarm system
- ☐ Satellite dish antenna
- ☐ Water treatment system
- ☐ Solar devices
- ☐ Major appliances
- ☐ Other____________________

Property Address:____________________ **Seller Initials_____** **Buyer Initials____** Page **2** of **7**

PROPERTY CONDITION DISCLOSURE FORM REPORT (SAMPLE PAGE 3OF 7)

YES	NO	UNK	N/A	D. MECHANICAL/ UTILITY SYSTEMS
☐	☐	☐	☐	15) Fuel type? ____________________ Are you aware of any heating system problem? If yes, explain:____________________
☐	☐	☐	☐	16) Hot water heater type? ________________________ Age: __________ Are you aware of any hot water problems? If yes, explain:____________________
☐	☐	☐	☐	17) Is there an underground storage tank? If yes, list the age of tank__________ and location:____________________
☐	☐	☐	☐	18) Are you aware of any problems with the underground storage tank? If yes, explain:____________________
☐	☐	☐	☐	19) During the time you have owned the property, has there ever been an underground storage tank located on the property? If yes, has it been removed? ☐ Yes ☐ No If yes, what was the date of removal________ and what was the name and address of the person or business who removed such underground storage tank? ____________________ Provide any and all written documentation of such removal within your control or possession by attaching a copy of such documentation to this form.
☐	☐	☐	☐	20) Air conditioning type?____________________ Are you aware of any air conditioning problems? If yes, explain:____________________
☐	☐	☐	☐	21) Plumbing system problems? If yes, explain:____________________
☐	☐	☐	☐	22) Electrical system problems? If yes, explain:____________________
☐	☐	☐	☐	23) Electronic security system problems? If yes, explain:____________________
☐	☐	☐	☐	24) Are there carbon monoxide or smoke detectors located in the dwelling on the property? If yes, state the number of detectors_____ and whether there have been problems with such detectors:____________________
☐	☐	☐	☐	25) Fire sprinkler system problems? If yes, explain:____________________

Property Address:____________________ **Seller Initials_____** **Buyer Initials____** Page **3** of **7**

YES	NO	UNK	N/A	E. WATER SYSTEM
☐	☐	☐	☐	26) Domestic water system type: ☐ Public; ☐ Private well; Other___________________________
				27) If public water:
☐	☐	☐	☐	a) Is there a separate expense/fee for water usage? If yes, is the expense/fee for water usage flat or metered?________ Provide the amount of the expense/fee_____________and explain: ____________________ ____________________
☐	☐	☐	☐	b) Are there unpaid water charges? If yes, state amount unpaid:________________________
				28) If private well:
☐	☐	☐	☐	Has the well water been tested for contaminants/volatile organic compounds? If yes, attach a copy of the report. If no report is available, provide name of entity that performed testing and describe results of such testing:____________________ ____________________ ____________________
☐	☐	☐	☐	If public water or private well: Are you aware of any problems with the well or with the water quality, quantity, recovery, or pressure? If yes, explain:________________________________ ____________________ ____________________

YES	NO	UNK	N/A	F. SEWAGE DISPOSAL SYSTEM
☐	☐	☐	☐	29) Sewage disposal system type: ☐ Public; ☐ Septic; ☐ Cesspool; Other:____________________ ____________________
				30) If public sewer:
☐	☐	☐	☐	a) Is there a separate charge made for sewer use? If yes, is it flat or metered?______________ ____________________
☐	☐	☐	☐	b) If it is a flat amount, state amount__________________ and due dates:________________ ____________________
☐	☐	☐	☐	c) Are there any unpaid sewer charges? If yes, state the amount:______________________
				31) If private:
☐	☐	☐	☐	a) Name of service company:____
☐	☐	☐	☐	b) Date last pumped:_________________________ Frequency of pumping during ownership: ____________________
☐	☐	☐	☐	c) For any sewage system, are there problems? If yes, explain:________________________ ____________________ ____________________

Property Address:____________________________________ **Seller Initials**_____ **Buyer Initials**____ Page **4** of **7**

PROPERTY CONDITION DISCLOSURE FORM REPORT (SAMPLE PAGE 5 OF 7)

YES	NO	UNK	N/A	G. ASBESTOS/ LEAD
☐	☐	☐	☐	32) Are asbestos insulation or building materials present? If yes, location:____________________ ____
☐	☐	☐	☐	33) Is lead paint present? If yes, location:____________________ ____
☐	☐	☐	☐	34) Is lead plumbing present? If yes, location:____________________ ____

YES	NO	UNK	N/A	H. BUILDING/ STRUCTURE/ IMPROVEMENTS
☐	☐	☐	☐	35) Is the foundation made of concrete? If no, explain:____________________ ____
☐	☐	☐	☐	36) Foundation/slab problems or settling? If yes, explain:____________________ ____ ____
☐	☐	☐	☐	37) Basement water seepage/dampness? If yes, explain amount, frequency and location:____________________ ____
☐	☐	☐	☐	38) Sump pump problems? If yes, explain:____________________ ____ ____
☐	☐	☐	☐	39) Do you have knowledge of any testing or inspection done by a licensed professional related to a foundation on the property? If yes, attach a copy of the report. If no report is available, provide name of entity that performed testing and describe results of such testing: ____________________ ____ ____ ____
☐	☐	☐	☐	40) Do you have knowledge of any repairs related to a foundation on the property? If yes, explain:____________________ ____
☐	☐	☐	☐	41) Roof type:____________________; Age:____________________
☐	☐	☐	☐	42) Roof leaks? If yes, explain:____________________ ____
☐	☐	☐	☐	43) Exterior siding problems? If yes, explain:____________________ ____
☐	☐	☐	☐	44) Chimney, fireplace, wood or coal stove problems? If yes, explain:____________________ ____
☐	☐	☐	☐	45) Patio/deck problems? If yes, explain:____________________ ____

Property Address:______________________________ **Seller Initials**_____ **Buyer Initials**____ Page **5** of **7**

PROPERTY CONDITION DISCLOSURE FORM REPORT (SAMPLE PAGE 6 OF 7)

YES	NO	UNK	N/A	H. BUILDING/ STRUCTURE/ IMPROVEMENTS (Continued)
☐	☐	☐	☐	46) If patio/deck is constructed of wood, is the wood treated or untreated? ____________________ ____________________
☐	☐	☐	☐	47) Driveway problems? If yes, explain:____________________ ____________________
☐	☐	☐	☐	48) Water drainage problems? If yes, explain:____________________ ____________________
☐	☐	☐	☐	49) Interior floor, wall and/or ceiling problems? If yes, explain:____________________ ____________________
☐	☐	☐	☐	50) Fire and/or smoke damage? If yes, explain:____________________ ____________________
☐	☐	☐	☐	51) Termite, insect, rodent or pest infestation problems? If yes, explain:____________________ ____________________
☐	☐	☐	☐	52) Rot or water damage problems? If yes, explain:____________________ ____________________
☐	☐	☐	☐	53) Is the structure(s) insulated? If yes, type: ____________________; location:____________ ____________________
☐	☐	☐	☐	54) Has a test for radon been performed? If yes, attach copy of the report. If no report is available, provide the name of entity that performed the testing and describe the results of such testing:____________________ ____________________ ____________________ ____________________
☐	☐	☐	☐	55) Is there a radon control system in place? If yes, explain:____________________ ____________________
☐	☐	☐	☐	56) Has a radon control system been in place in the previous 12 months? If yes, explain:___________ ____________________ ____________________

The seller should attach additional pages, if necessary, to further explain any item(s) above. Indicate here the number of additional pages attached: ______

Questions or Comments? Consumer Problems? Visit the Department of Consumer Protection website at: www.ct.gov/dcp

Property Address:____________________ **Seller Initials_____** **Buyer Initials____** Page **6** of **7**

PROPERTY CONDITION DISCLOSURE FORM REPORT (SAMPLE PAGE 7 OF 7)

IMPORTANT INFORMATION

(A) Responsibilities of Real Estate Brokers

This report in no way relieves a real estate broker of his or her obligation under the provisions of section 20-328-5a of the Regulations of Connecticut State Agencies to disclose any material facts. Failure to do so could result in punitive action taken against the broker, such as fines, suspension or revocation of license.

(B) Statements Not to Constitute a Warranty

Any representations made by the seller on the written residential property condition disclosure report shall not constitute a warranty to the buyer.

(C) Nature of Disclosure Report

This Residential Property Condition Disclosure Report is not a substitute for inspections, tests, and other methods of determining the physical condition of the property.

(D) Information on the Residence of Convicted Felons

Information concerning the residence address of a person convicted of a crime may be available from law enforcement agencies or the Department of Public Safety.

(E) Building Permits and Certificates of Occupancy

Prospective buyers should consult with the municipal building official in the municipality in which the property is located to confirm that building permits and certificates of occupancy have been issued for work on the property.

(F) Home Inspection

Buyers should have the property inspected by a licensed home inspector.

(G) Concrete Foundation

Prospective buyers may have a concrete foundation inspected by a licensed professional engineer who is a structural engineer for deterioration of the foundation due to the presence of pyrrhotite.

(H) Buyer's Certification

The buyer is urged to carefully inspect the property and, if desired, to have the property inspected by an expert. The buyer understands that there are areas of the property for which the seller has no knowledge and this disclosure statement does not encompass those areas. The buyer also acknowledges that the buyer has read and received a signed copy of this statement from the seller or seller's agent.

Date_______________ **Buyer**__________________________________ **Buyer**__________________________________
Signature **Print Name**

Date_______________ **Buyer**__________________________________ **Buyer**__________________________________
Signature **Print Name**

(I) Seller's Certification

To the extent of the seller(s) knowledge as a property owner, the seller acknowledges that the information contained above is true and accurate for those areas of the property listed. In the event a real estate broker or salesperson is utilized, the seller authorizes the brokers or salespersons to provide the above information to prospective buyers, selling agents or buyer's agents.

Date_______________ **Seller**__________________________________ **Seller**__________________________________
Signature **Print Name**

Date_______________ **Seller**__________________________________ **Seller**__________________________________
Signature **Print Name**

Property Address:__________________________________ **Seller Initials**_____ **Buyer Initials**____ Page **7** of **7**

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TOPIC 6

Appraisal:
Valuation & Market Analysis

EXAM TOPICS:

A. Appraisals

1. Purpose and use of appraisals for valuation (pp. 6-1~ 6-2)
2. General steps in appraisal process (pp. 6-9~ 6-10) (pp. 6-17~6-18)
3. Situations requiring appraisal by certified appraiser (pp. 6-2~ 6-3)

B. Estimating Value (pp. 6-3)

1. Effect of economic principles and property characteristics (pp. 6-3~ 6-4)
2. Sales or market comparison approach (pp. 6-10~ 6-12)
3. Cost approach (pp. 6-12~ 6-14)
4. Income analysis approach (pp. 6-14~ 6-15)

C. Competitive/Comparative Market Analysis (pp. 6-25)

1. Selecting comparables (pp. 6-25)
2. Adjusting comparables (pp. 6-25)

Appraisal Industry

A. Property appraisals came into question and were in part causation of unsound real estate investments surrounding the **Savings and Loan Association** crisis collapse. The 1989 1,000+ **Savings and Loan Bank Crisis** and failures were one of the most significant collapses since the 1929 **Great Depression** and the **FSLIC** (Federal Savings & Loan Insurance Corporation) paid S&L's some $20 billion to depositors before going bankrupt. This S&L collapse contributed to the unsound home investments and questionable real property appraisals.

B. Appraisal regulation was introduced by Congress via passing FIRREA, the Financial Institutions Reform Recovery and Enforcement Act of 1989 in the wake of the savings and loan crisis which also established the Resolution Trust Corporation (RTC) and closing hundreds of insolvent S&Ls funding payout insurance to depositors.

C. Appraisals performed as part of a federally related transaction must comply with state standards and must be performed by a state-certified or state-licensed appraiser.
D. State appraiser licensing requirements and appraisal standards must meet minimu levels set by the **Appraisal Standards Board** and **Appraisal Qualifications Board** of the Appraisal Foundation, a national group of representatives of major appraisal and related organizations.
E. **Appraisal Foundation**, a national group of representatives of major appraisal and related organizations.

Appraisal Industry

- The collapse of many savings and loan associations as a result of the surge into unsound
  investments were at least partly the consequence of questionable property appraisals.
- Congress introduced appraisal regulation by passing **FIRREA** in 1989.
- Appraisals performed as part of a federally related transaction must comply with state standards and must be performed by a state-certified or state-licensed appraiser.
- State appraiser licensing requirements and appraisal standards must meet minimum levels set by the **Appraisal Standards Board** and **Appraisal Qualifications Board** of the
- **Appraisal Foundation**, a national group of representatives of major appraisal and related
  organizations.

Appraisal Purpose & Use of Appraisals for Valuation

A. The collapse of many savings and loan associations as a result of the surge into unsound investments was at least partly the consequence of questionable property appraisals.
B. Congress introduced appraisal regulation by passing FIRREA in 1989.
C. Appraisals performed as part of a federally related transaction must comply with state standards and must be performed by a state-certified or state-licensed appraiser.
D. State appraiser licensing requirements and appraisal standards must meet minimum levels set by the Appraisal Standards Board and Appraisal Qualifications Board of the Appraisal Foundation, a national group of representatives of major appraisal and related organizations.

Situations Requiring Appraisal via Certified Appraiser (Residential | General)

A. All transactions of $ 1,000,000 or more
B. Non-residential and residential (other than one- to four-family) trans- actions of $250,000 or more
C. Complex residential transactions of $250,000 or more

1. A regulated institution may presume that appraisals of one- to four-family residential properties are not complex, unless the institution has readily available information that a given appraisal will be complex.
2. The regulated institution is responsible for making the final determination of whether the appraisal is complex.

   EXAMPLE: An example of a complex appraisal would be an appraisal of a commercial property in the center of a residential neighborhood.

EFFECT OF ECONOMIC PRINCIPLES AND PROPERTY CHARACTERISTICS

PHYSICAL CHARACTERISTICS AFFECTING VALUE

1. **DURABILITY: (INDESTRUCTIBLE)** Although improvements depreciate physically over time, land does not.

   Example: Buy some land and let it sit for 30 years and then come back to check on it, it still looks the same. Even a brick building may still look the same. This feature increases the value of real estate.

2. **IMMOBILITY:** Real estate is not movable.

   Example: have you heard that the 3 most important aspect of real estate value is location, location, location. Immobility can be good or bad because if your property is in a good location, that will bring its value upwards. But if it‘s in a bad location, you cannot move it elsewhere.

3. **HETEROGENEITY (UNIQUE)** (non-homogeneity): Every property is Unique; No two parcels are alike.

   Even when you have two adjacent lots in the subdivision that would seem to be of the same size and value, they still have two different legal descriptions; one is lot #17 while the other is lot #18.

ECONOMIC CHARACTERISTICS AFFECTING VALUE (D.U.S.T)

1. **DESIRABILITY (DEMAND):** Whether or not there are possible buyers interested in the property that are willing, able, and have the financial means to purchase.

   Example: 200-unit condominium complex is built on a waterfront; some units are not facing the water. Chances are that the units facing the water will sell at a higher price because they are more desirable, i.e. there is more ―demand‖ on them.

2. **SCARCITY (SUPPLY):** Whether or not there are other similar properties of a comparable nature within the same general area that will compete with the subject property.

   Example: a 200 unit condominium complex was pre-sold before construction; finally one buyer canceled his purchase agreement because he was being transferred out of town. When your buyer wants to make an offer on the last remaining unit, it will be very hard to bargain on the price because of scarcity. Had it been the other way around, for example, if only 50 units were sold and there were 150 units left on the market, there will be some room for bargaining and the price may go down.

3. **UTILITY:** The type of use that the subject property is most suitable for, and whether or not it satisfies the needs of a certain buyer.

Example: a small town known for its large retirement community has a new subdivision being built with mostly one-story Ranch homes. This design will probably prove to be popular with the majority of people in the city, because those of a retirement age may have issues with climbing too many stairs, therefore they will be able to ―utilize‖ this type of design much better than a two-story home, especially with bedrooms located upstairs.

4. **TRANSFERABILITY:** The ability to sell, lease, will property to another person. The more the restrictions on the sale, lease or transfer of property, the less the value.

Example: Property may be the subject of a dispute between partners, or certain action taken by a government entity such as the IRS or DEA, therefore, unless these restrictions are lifted, property will either have a lower value or no value at all.

Appraisal Definition

Real estate appraisal, property valuation or land valuation is the process of developing an opinion of value, for property (usually market value) by a state licensed appraiser. Real estate transactions often require appraisals because they occur infrequently and every property is unique (especially their condition, a key factor in valuation), unlike corporate stocks, which are traded daily and are identical. The location also plays a key role in valuation. However, since property cannot change location, it is often the upgrades or improvements to the home that can change its value. Appraisal market valuation reports form the basis for mortgage loans, settling estates and divorces, taxation, and so on. Sometimes an appraisal report is used to establish a sale price for a property.

D. Value

1. **Definition -** the present worth of future benefits arising from the ownership of real property.

2.Characteristics necessary for a property to have value in the real estate market include “DUST”:

a.Demand—need supported by purchasing power.

b. Utility—capacity to satisfy human wants and needs.

c. Scarcity— finite supply.

d. Transferability—transfer of ownership rights with relative ease.

E. Market value

1. Most probable price a property will bring in a competitive market, allowing for

reasonable time to find a knowledgeable purchaser.

a. The buyer and seller are not under pressure to act.

b. Payment is made in cash or equivalent.

2. Typical goal of an appraiser, although a property may have different values at the same time.

3. Estimated price (compare to market price, which is the actual selling price).

A. Market value and market price

1. Market value

a. Most probable price a property will bring in a competitive market, allowing for reasonable time to find a knowledgeable purchaser.
   1. The buyer and seller are not under pressure to act.
   2. Payment is made in cash or equivalent.

b. Typical goal of an appraiser, although a property may have dif- ferent values at the same time

c. Estimated price (compare to market price, which is the actual selling price)

2. Market price

a. Market price is the “last price the property sold for” which may be recent or serveral years in the past.

b. Market price would be the same if the property was recently sold (last 6months ~1year) and is most relevant whereas properties sold 5~30 years ago would have a less relevant market price meaning, use and value.

MARKET VALUE or OMV (**Open Market Valuation**) is the price at which an asset would trade in a competitive auction setting. Market value is often used interchangeably with open market value, fair value or fair market value, although these terms have distinct definitions in different standards, and may or may not differ in some circumstances.

Search Results

Open Market Value is the estimated amount that a property would exchange contracts at (sell for) between a willing buyer and a willing buyer on the date of the **valuation**. In the opinion of the valuer, it is the probable price which a property would be expected to achieve on the day in a **open** fair sale environment.

Market value or OMV (Open Market Valuation) is the price at which an asset would trade in a competitive auction setting. Market value is often used interchangeably with open market value, fair value or fair market value, although these terms have distinct definitions in different standards, and may or may not differ in some circumstances.

Market value is the most commonly used type of value in real estate appraisal in the United States because it is required for all federally regulated mortgage transactions, and because it has been accepted by US courts as valid. However, real estate appraisers use many other definitions of value in other situations.

OPEN MARKET VALUE (OMV) is an opinion of the best price at which the sale of an interest in an asset would have been completed unconditionally for cash consideration on the date of valuation, assuming:

a. willing seller;

b. that, prior to the date of valuation, there had been a reasonable period (having regard to the nature of the asset and state of the market) for the proper marketing of the interest, for the agreement of price and terms and for the completion of the sale;

c. that the state of the market, level of values and other circumstances were, on any earlier assumed date of exchange of contracts, the same as on the date of valuation;

d. that no account is taken of any additional bid by a purchaser with a special interest; and

e. that both parties to the transaction had acted knowledgeably, prudently and without compulsion.

FAIR MARKET VALUE (**FMV**) is an estimate of the market value of a property, based on what a knowledgeable, willing, and unpressured buyer would probably pay to a knowledgeable, willing, and unpressured seller in the market. An estimate of fair market value may be founded either on precedent or extrapolation. Fair market value differs from the intrinsic value that an individual may place on the same asset based on their own preferences and circumstances.

A home's fair market value is the price it would sell for in a perfectly logical world—one where both home buyer and seller are acting of their own free will (in other words, they aren't desperate to make a sale) and are reasonably aware of a home's good and bad points, and where the buyer could just as easily choose a different house that suits her needs better.

In such a world, market forces reign. Buyers and sellers negotiate up or down from their various positions and agree on a home's price. Deal done. All is good!

A home's *fair market value* is comparable to a home's *market value*—what it would fetch on the open market—but is used in special circumstances where the concept of fairness is important to evoke so that the home's sales price carries more weight.

Here are some circumstances where you'll likely hear about the fair market value of a home:

- **Property tax assessments -** in a specific market are based on a home value and comparable properties.
- **Home insurance claims**—if a house suffers damage from a fire, flood, or other disaster, the insurer will look to the market value to determine a compensation estimate.

- **Refinancing a home loan**—the bank will typically use an appraisal of a home's current market value as a measure of the home value to determine refinancing terms for a mortgage.
- **Estate sales**—if the homeowner has died and a relative wants to purchase the property, the court will look at home value appraisal to determine a price for the sale.
- If the government wants to "buy out" a homeowner to use that land to, say, build a highway or school, the owner is typically entitled to be compensated at fair market value so that she will sell.
- **Short sale**—this is when a home is worth less than the owners owe on their mortgage. In this case, the owners must persuade the lender to let them sell the home for some amount that is less than the balance of the home loan they still owe. "When a bank does allow this, the bank wants to make sure that the short-selling purchase price is at least FMV for the property," says Pellegrini. Because, of course, no one likes a total loss on a home value!

FAIR MARKET VALUE DEFINITION AND USE

- The fair market value is the price an asset would sell for on the open market when certain conditions are met.
- The conditions are: the parties involved are aware of all the facts, are acting in their own interest, are free of any pressure to buy or sell, and have ample time to make the decision.
- Fair market value is different than market value and appraised value.
- Tax settings and the real estate market are two areas that commonly use fair market value.
- Insurance companies use fair market value in determining certain claim payouts.

ARM'S LENGTH TRANSACTION: A transaction that occurs in a competitive market that leads to a fair sale involving a willing buyer and seller, both acting with knowledge of the property under no duress and with no other intervening factors such as selling to a relative or friend.

An arm's length transaction, also known as the arm's length principle (ALP), indicates a transaction between two independent parties in which both parties are acting in their own self-interest. ... In contract law, from the opposing party, and are acting in their own self-interest to attain the most beneficial deal.

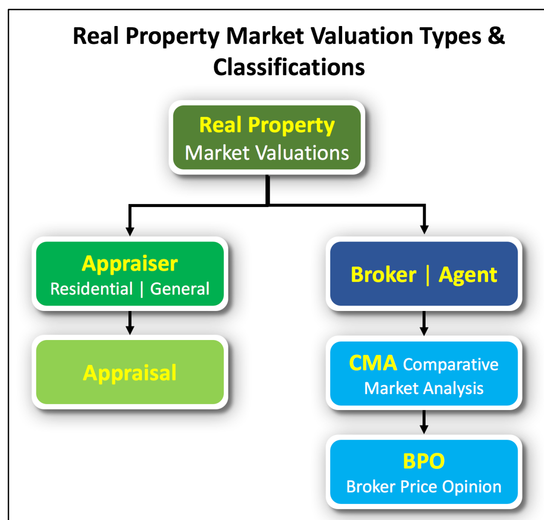
- The parties involved in an arm's length sale usually have no pre-existing relationship with each other.
- These types of deals in real estate help ensure that properties are priced at their fair market value.

- Deals between family members or companies with related shareholders are not considered arm's length transactions.

Types of Appraisals (Broker | Agents and Appraisers)

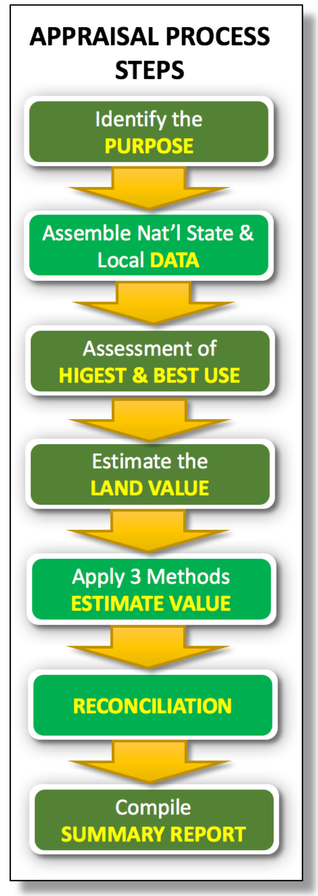
A. **Appraisal**—an opinion of value; a detailed estimate of a property's value by a professional appraiser.
B. **Competitive/Comparable market analysis (CMA)—**used by the broker or the salesperson to help the seller determine a listing price for the property; basically, a comparison of prices of recently sold and currently for sale properties that are similar in location, style, and amenities to the property of the listing seller. CMA will generally estimate market value as likely to fall within a range of figures. CMAs can also guide a purchaser in formulating an offer.
C. **Broker Price Opinion (BPO)—**similar to a CMA but different in that it is usually more detailed because it is used by a third party (e.g., a relocation company) to provide a basis for negotiation of a purchase price or a buyout in the case of a company employee being transferred to another city. The BPO is generally more detailed because the third party knows very little about the neighborhood in which the property is located. Real estate brokers are paid to complete BPOs.

CMA – Comparable or Competitive Market Analysis - A comparative market analysis is an examination of the prices at which similar properties in the same area recently sold. Real estate agents perform a comparative market analysis for their clients to help them determine a price to list when selling a home or a price to offer when buying a home. Since no two properties are identical, agents make adjustments for the differences between the sold properties and the one that is about to be purchased or listed to determine a fair offer or sale price. Essentially, a comparative market analysis is a less-sophisticated version of a formal, professional appraisal.



BPO – Broker Price Opinion - + When doing a BPO, the real estate pro researches the 'subject property,' they take pictures of it, they also scope out the neighborhood as well as pull 6 comparable properties (3 Active Comps and 3 Sold Comps) in their MLS (Multiple Listing Service). They then take all of this information, the pictures they took of the subject and their knowledge of the local real estate market and they input it into a BPO form. The final BPO is used to support their professional opinion that will help determine the potential selling price[1] or estimated value[2] of a real estate property.

Steps in the Appraisal Process



Purpose. The first step in the process is to define the appraisal problem and the purpose of the appraisal. This involves

- identifying the subject property by legal description
- specifying the interest to be appraised
- specifying the purpose of the appraisal, for example, to identify market value for a purchase, identify rental levels, or establish a value as collateral for a loan
- specifying the date for which the appraisal is valid
- identifying the type of value to be estimated

Data Collection. The second step is to collect, organize and analyze relevant data about the subject property. Information relevant to the property includes notes and drawings from physical inspection of the subject, public tax and title records, and reproduction costs. Relevant information about the market includes environmental, demographic, and economic reports concerning the neighborhood, community, and region.

Highest and best use. The third step is to analyze market conditions to identify the most profitable use for the subject property. This use may or may not be the existing use.

Land value. The fourth step is to estimate the land value of the subject. An appraiser does this by comparing the subject site, but not its buildings, with similar sites in the area, and making adjustments for significant differences.

Three approaches. The fifth step is to apply the three basic approaches to value to the subject: the sales comparison approach, the cost approach, and the income capitalization approach. Using multiple methods serves to guard against errors and to set a range of values for the final estimate.

Reconciliation. The sixth step is to reconcile the value estimates produced by the three approaches to value into a final value estimate. To do this, an appraiser must:

- weigh the appropriateness of a particular approach to the type of property being appraised
- take into account the quality and quantity of data obtained in each method

Summary Report. The final step is to present the estimate of value in the format requested by the client.

APPRAISAL - A real estate appraisal that must comply with the **Uniform Standards of Professional Appraisal Practice (USPAP)** is a standard procedural component of the real estate transaction enabling both parties in the real estate transaction to understand the fair market value of the real property. The real property 'value' determined is often used for property financing or refinancing, home equity loans and credit lines. There are three primary types of real estate appraisals that may be used, including the "**sales comparison**

approach", the "**cost approach**", and the "**income capitalization approach**".

In the process of buying or selling a home, you may hear some strange and vaguely familiar terms. One of these terms is the "real estate appraisal report." This is a written report that estimates the current fair market value of the property that you are buying or selling.

What Information Determines the Report?

The price given in the appraisal is determined by several factors:

- Recent sales of similar properties in the area
- Current condition of the property
- The neighborhood and its impact on future value

These terms are just vague enough to be difficult for many buyers and sellers to understand.

Recent Sales

An appraiser will review the records of nearby properties sold from the last few weeks or months to find three or four that are similar in size, style and layout. The selling prices of those homes will help determine the value of the home being appraised. Many buyers and sellers want to know how recently the comparable homes were sold, and what is defined as "within the same area."

The parameters vary between homes in a metropolitan area and in a rural community. In a larger city, the appraiser could find similar homes that sold in the last month and within one mile of the home that is for sale. In a small town or rural community, that appraiser may have to consider sales over several months or widen the perimeter to encompass the entire town or several miles.

Current Condition

An appraiser must evaluate the current condition of the selling property to determine its value. He or she will inspect the home for any health and safety issues. Any violations or risks will be noted in the final report. These may include old wiring, a lack of railing along stairs and many other conditions. In addition, the appraiser will evaluate the overall design of the home. Is it comparable to others in the neighborhood or is it above or below them? A home that needs serious updating will have a lower appraisal value than one that has recently been renovated.

The Neighborhood

The surrounding neighborhood also plays a part in the appraisal. The appraiser must determine the current state of the neighborhood and where it is headed in the future. For instance, a home in a new or up-and-coming subdivision will have a higher value today, because it is expected to increase in the future. On the other hand, a home in a tired-looking neighborhood that is declining instead of growing doesn't have the same potential for value.

SALES COMPARISON APPROACH METHOD

The "**SALES COMPARISON**" real estate appraisal approach is more typically performed on residential type properties. This approach compares the price per unit area of similar properties in the surrounding area. The price variations are generally averaged to create a fair market value for the property being appraised. This type of real estate appraisal is considered to be the most accurate appraisal as it utilizes recent market values on comparable properties.

B. Market/data approach (sales comparison or direct sales)

1. A value estimate is obtained by comparing the subject property with recent sales of comparable properties through adjustment of sales prices of comparables. Comparable properties used in an analysis should be "arm's length" or a normal market transaction involving willing buyers and willing sellers, as opposed to a foreclosure sale, an auction, or a sale to a relative.
2. Four areas of adjustment:
   a. Date of sale
   b. Location
   c. Physical characteristics
   d. Terms of the sale
3. The adjustment process involves three basic steps:
   a. Adjust the price of the comparable for any difference between the comparable and the subject property (the property being appraised). With your dollar adjustments remember to always mirror your subject property.
   b. **C.B.S.** - Comparable better subtract from the comparable the difference between the comparable and the subject property.
   c. **S.B.A.** - Subject better add to the comparable the difference between the comparable and the subject property.
4. Considered the most reliable of the three approaches in appraising residential property.

SALES OR MARKET COMPARISON APPROACH

A. Also known as THE MARKET DATA APPROACH
B. Most suitable for PRE-OCCUPIED HOUSES AND VACANT LAND.
C. Value is estimated by using other comparable property that has been recently sold in the same general area. If the sold comparable has a superior feature in comparison to the subject property, then it is adjusted downwards, but if it has an inferior feature then it is adjusted upwards.
D. Appraiser gives emphasis to normal inflation, age of improvements, square footage, any good or bad features such as a garage, basement, bathrooms, fireplace, cracked foundation, evidence of termite infestation, etc.

Note: The best comparable is a SOLD comparable

Example: You are required to evaluate the subject property that has 2,800 sq. ft. and is similar to the sold comparable. The subject property does not have a garage. One square foot is worth $120 and a 2 car garage is worth $10,000.

Has 300 sq. ft. extra

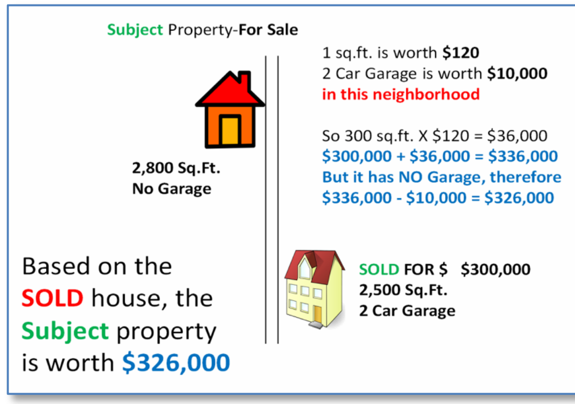
300 sq. ft. X $120 = $36,000

$300,000 + $36,000 = $336,000

But it has NO garage

$336,000 - $10,000 = $326,000

Based on the sold property, **the subject property is worth $326,000**



E. When comparing property to others sold, at least 3 to 4 SOLD properties should be selected to compare instead of comparing to one only which may have been sold at exceptionally favorable terms or under duress.

F. Always compare apples to apples. If one property is situated on a lakefront, do not use the comparable that is across the street with only "***lake access***". If you have a one-story home, do not compare it to a two-story or a quad level home.

COST MODEL | REPLACEMENT OR SUMMATION APPROACH

The "**COST MODEL**" method approach will take the value the land less any depreciated man-made or artificial improvements. Those man-made/artificial 'improvements' refer to the new construction costs of the improvements on the land. Typical real estate appraisals using this method begin with a replacement cost (or reproduction cost) and then subtract value for any encumbrances (burden's) relating to the land or the issues with the man made/artificial improvements. This method is typically performed on historical real properties, barns, other non-standard real properties.

A. Cost approach

1. **Based on the principle of substitution**
2. **Steps of cost approach**
    a. Estimate the land value.
    b. Estimate the replacement cost of the improvements.
    c. Estimate the depreciation.
    d. Deduct the depreciation from the replacement cost.
    e. Add the land value to the depreciated cost of improvements—do not depreciate land.
3. **Depreciation**—generally applies to a wasting asset, such as a building

a. **Physical deterioration** (wear, tear, poor maintenance)—may be curable
b. or incurable.
c. **Functional obsolescence**—may be curable or incurable (outdated
d. items, poor design).
e. **External obsolescence** (economic, environmental, or locational)—loss
f. of value due to factors outside the property: is always incurable.
g. Most reliable approach for special-purpose buildings such as churches
h. and schools.

Most suitable for new property and property with little or no comparables, such as a museum, library, school, etc. In this method, the appraiser takes the following steps to appraise the property:

A. Land is appraised without the building, using the market comparison approach.
B. The cost of reconstructing the building as a new unit is estimated.
C. The value of the land is then added to the value of the building.
D. **REPRODUCTION COST** - Is the cost to reproduce an exact duplicate of the same building using current materials and methods to produce a functional equivalent of the subject property.
E. **REPLACEMENT COST** - The cost of replacing a building with another that functions in a similar way but not a duplicate. This method is more suitable for appraising older structures since it may not be possible to find discontinued building material that would be used at the present time such as asbestos insulation or plumbing fixtures of a certain type.
F. **DEFERRED MAINTENANCE** - Existing maintenance and repair requirements that were due but put off.
G. **ACCRUED DEPRECIATION** - The amount of depreciation that has occurred between the time the improvement was built and the effective date of the appraisal.
F. **ECONOMIC LIFE** - Is the period of time during which the structure is expected to remain useful in its original function. This period is essential to calculating accrued depreciation.

The Cost Approach

Ex: New construction surrounded by existing older homes

Step:1 What is the land worth Without the house?

The market comparison (market data)approach is used to determine the land value.

For example: $70,000

3,000 s.f. NEW home

We must determine The cost of **NEW Construction.** For example **$120/s.f.**

3000 s.f. x $120 = $360,000 for the NEW construction

+ **$70,000** for land

= $430,000

METHODS OF DEPRECIATION (FOR MAN-MADE IMPROVEMENTS)

1. **PHYSICAL DETERIORATION:** Ordinary wear-and-tear such as roof leaks, problem with plumbing, electrical wiring, basement cracks, etc.
2. **FUNCTIONAL OBSOLESCENCE:** Outdated design and layout inadequacy, property may have served its purpose in the past but does not meet modern requirements such as commercial building that lacks parking, 4-bedroom house with one bathroom, etc.
3. **EXTERNAL (economic, environmental) OBSOLESCENCE**: Loss of value due to changes in society and the surrounding area such as presence of crime in neighborhood, pollution from factories, noise from airport, high unemployment, etc.

CURABLE OBSOLESCENCE: Can be corrected. Example, a house with no garage may have a large enough lot to add a two-car garage.

INCURABLE OBSOLESCENCE: Cannot be or not economically feasible to be corrected or modified. External obsolescence is considered to be the hardest to cure.

INCOME ANALYSIS APPROACH METHOD

CAPITALIZATION METHOD (BROKER ONLY)

The "**income capitalization approach**" to real estate is primarily used for commercial properties and to a lesser extent industrial, mixed properties and is based on the expectation of future benefits. This appraisal method type utilizes models to predict the behavior of market participants, in particular with regard to income-producing commercial properties. It is based on the expectation of future benefits. The "income capitalization approach" relates 'value' to 'market rent' that real property can be expected to earn and to the 'resale value'. In brief, this approach converts 'income' into value; the more the rent income, the more the property is worth.

Income capitalization approach

1. Based on the present value of the rights to future income
2. Steps in the income approach
    a. Estimate the annual potential gross income.
    b. Deduct the vacancy and rent loss to arrive at the effective gross
    c. income.
    d. Deduct the annual operating expenses to arrive at the annual net
    e. operating income.
    f. Estimate the capitalization rate.
    g. Apply the capitalization rate to the annual net income.
3. Formula for capitalization rate: net income ÷ capitalization rate = value.
4. As risk increases, the rate of return increases and the value decreases, and as the risk decreases, the rate of return decreases, the value increases and vice versa.
5. **Gross rent multiplier (GRM)**
    a. Used as a substitute for the income approach in appraising a single-family home.
    b. Formula for GRM: sales price ÷ monthly rental income = GRM.
    c. Monthly rental income × GRM = estimated market value.
6. **Gross income multiplier (GIM)**
    a. Used as a quick way to appraise commercial and industrial properties.
    b. **Formula for GIM**: sales price ÷ annual rental income = GIM.
7. Most reliable approach for income-producing property.

INCOME APPROACH DETAIL

1. Used to estimate value of income property.
2. **VALUE** = NET OPERATING INCOME ÷ CAPITALIZATION RATE.
    A. **NET OPERATING INCOME (NOI)** = GROSS RENT - OPERATING EXPENSES
        I. GROSS RENT: Potential annual projected gross income - Vacancy and rent loss + Additional income
        II. OPERATING EXPENSES: Necessary annual costs to operate the project such as taxes, maintenance, insurance, utilities and management fees. Although interest is an expense, it is not considered an operating expense; neither are the vacancy factor, principal payments, capital improvements or special assessments.
        Note: **LOAN PAYMENTS** are known as DEBT SERVICE, which include principal and interest. They are not included in calculating the net operating expenses.

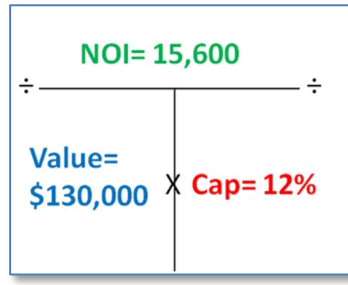
B. **CAPITALIZATION (CAP) RATE:** The rate of return an investor would receive on investment.

Example (1): What is the NOI if the gross rent for the year was $55,000 and the following expenses were considered:

Taxes: $4000/year, Insurance: $3000/year, Utilities: 500/month?

Answer: UTILITIES: $500 X 12 = $6000/YEAR

$55000 - $4000 - $3000 - $6000 = $42,000 **NOI**



Example (2): An investor is looking at a rate of return of 12% annually on his/her investment. The property has a gross income of $26,000/yr. with estimated expenses of 40% of gross/yr. How much should this investor pay for this property?

Answer: NOI = $26,000 - 40% = $15,600

$15,600 ÷ 12% = $130,000

Example (3): In the previous example, if the appraiser estimates that the Cap Rate in that market should be 10%, what would the value?

Answer: $15,600 ÷ 10% = $156,000

Example (4): in the previous example, if the appraiser estimates the Cap Rate to be 8%, what would the value be?

Answer: $15,600 ÷ 8% = $195,000

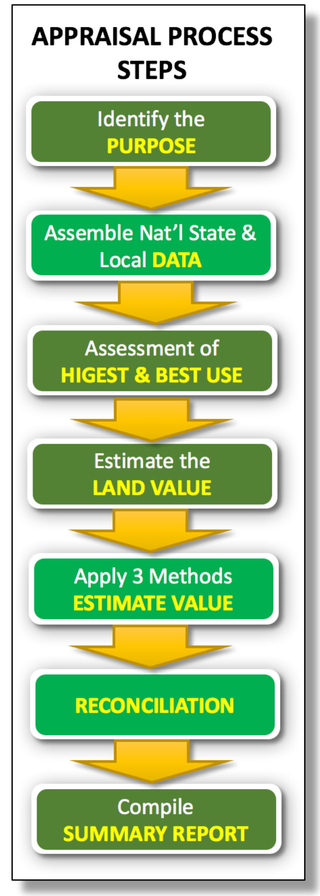
APPRAISAL PROCESS

A systematic procedure enables an appraiser to collect, organize and analyze the necessary data to produce an appraisal report.

DIFFERENCES BETWEEN CMA - BPO - APPRAISAL

	Created by	*Created or Positioned For*	*Purpose & Reason*	*Fee or Chargable*	*FAIR SUBJECTIVE OR OBJECTIVE*	*NUMBER OF PAGES*	*SPECIFIC FORMS*	*ORGANIZATIONAL CONTROL*	*METHODS*	*TIME TO CREATE / COMPLETE*
CMA Comparable Market Analysis	Broker or Salesperson	Buyer or Seller	Solicit a Listing	Free *(can Charge***)*	Subjective and Biased	2-4 or 5-40 typical	None	NONE user discretion	One	20-min
BPO Broker Price Opinion	Broker or Salesperson	Lender	Solicit a Listing	~$50-$185 each	Subjective and Biased	2-4 pages total	2-page Lender form	Lender and Gov't	oOne	1-2 hours
APPRAISAL Market Valuation	Appraiser Only	Lender Buyer or Seller	Property Market Valuation	~$400-$1.2K (Res) $800-$3K (Com)	Objective Fair & Honest	30-40 pages typical	8 page USPAP Form	USPAP	All Three	1-1.5 weeks
				*** if property is sold then Brokerage must refund fee						

Steps in the Appraisal Process



Purpose. The first step in the process is to define the appraisal problem and the purpose of the appraisal. This involves

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- specifying the date for which the appraisal is valid
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Data Collection. The second step is to collect, organize and analyze relevant data about the subject property. Information relevant to the property includes notes and drawings from physical inspection of the subject, public tax and title records, and reproduction costs. Relevant information about the market includes environmental, demographic, and economic reports concerning the neighborhood, community, and region.

Highest and best use. The third step is to analyze market conditions to identify the most profitable use for the subject property. This use may or may not be the existing use.

Land value. The fourth step is to estimate the land value of the subject. An appraiser does this by comparing the subject site, but not its buildings, with similar sites in the area, and making adjustments for significant differences.

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Summary Report. The final step is to present the estimate of value in the format requested by the client.

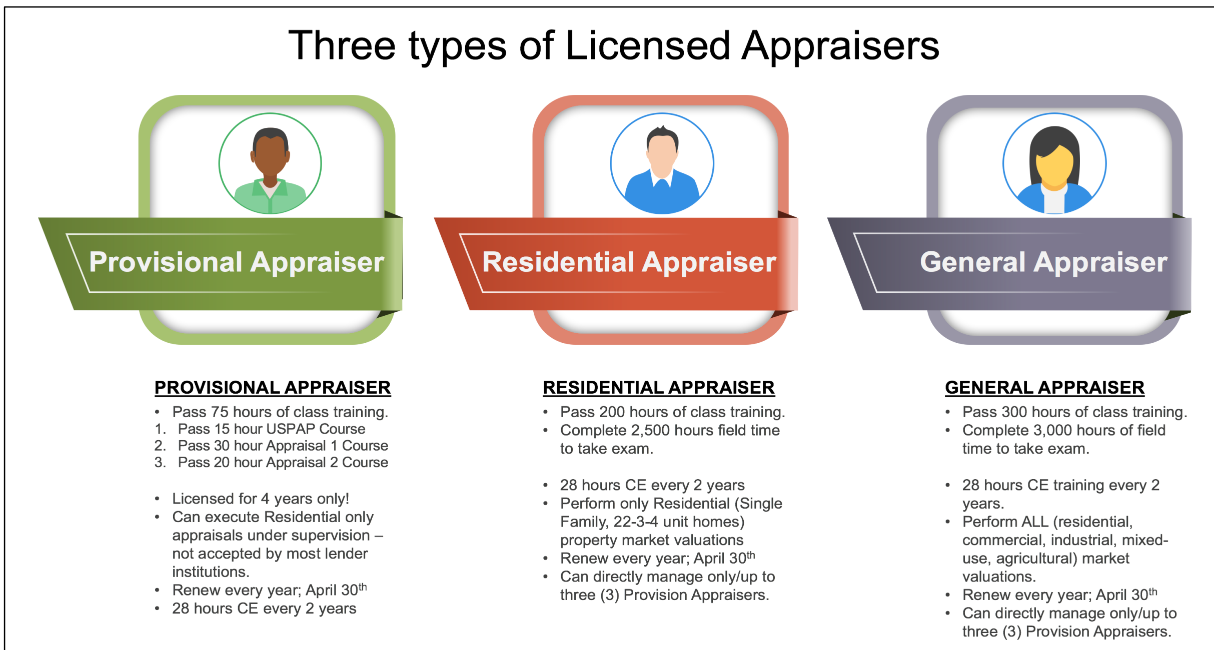
Types of Appraisers

There are three (3) types of real property appraisers which are **Provisional, Residential and General Appraiser**.

Provisional Appraiser is an apprentice and must work directly under supervision of the Residential or General Appraiser. This type of appraiser has only a four(4) year term and must move to Residential Appraiser level to continue. Generally, most lending institutions do not accept Provisional Appraisals (without Residential/General co-sign the appraisal document).

Residential Appraiser is a one who has 250 hours of in class training and 2,500 hours of field work experience (provisional level typically) and performs 28-hour CE (Continuous Education) every two even years. Residential only properties such as single family, 2-3-4 unit properties are completed under this type of appraiser.

General Appraiser is a one who has 300 hours of in class training and 3,000 hours of field work experience (provisional level typically) and performs 28-hour CE (Continuous Education) every two even years. The General Appraiser can appraise any type of property including residential, commercial, industrial agricultural, mixed-use and special purpose (churches, cemeteries, schools, etc.)



Capitalization Rate

Capitalization rate or "***cap rate***" is a measure of the ratio between the net operating income produced by an asset (usually real estate) and its capital cost (the original price paid to buy the asset), or alternatively its current market value. The rate is calculated in a simple fashion as follows:

Calculating the Capitalization (Cap Rate)

GROSS INCOME:
$270,000 per year (15 Apts @ $1,500/mo. * 12 mo.)
(this is 15-unit apartment building @ **$875K**)

How to calculate Net Income:

$270,000 (Gross Income annual)
-$15,000 (Taxes per year)
-$9,000 (Maintenance per year)
-$21,000 (Insurance)
= $225,000 (NET INCOME)

NET INCOME / PURCHASE PRICE = CAP RATE
$225,000 / $875,000 = 0.257 = 25.7%

Typical Terms and definitions:

Market Price is the last price the real property has sold for which could be several years. When a real property has recently sold, the Market Price and the Selling price are the same. When a property is for sale, the Market Price is the price the property last sold for. When the property sells, the Selling Price is the recent sales price and at that time matches the Market price.

Selling Price is the price that a real property as most recently sold for. This term refers more exclusively the recent sale price of the real property. The previous sale price (generally 2-40 years) is the Market Price.

Asking Price is the price that a seller wishes to sell the real property for. This often differs from the actual 'list price' that is found on the listing, MLS (**Multiple Listing Service**) or fair open market listed price. The seller in many cases has a more sentimental and higher value opinion and this sometimes is referred to as the '***dream price'***.

List Price is the price of a real property for sale set by the seller and licensed real estate listing agent. The List Price is the agreed price between what the seller and CMA (comparative/comparable market analysis) price provides.

Comparative Market Analysis is an examination of the prices at which similar properties in the same area recently sold. Real estate agents perform a comparative/comparable market analysis for their clients (signed to listing agreement) to help them determine a price to list when selling a home or a price to offer when buying a home.

Selling Price is the price that a real property as most recently sold for. This term refers more exclusively the recent sale price of the real property. The previous sale price (generally 2-40 years) is the Market Price.

TYPES OF VALUE

The purpose of an appraisal influences an estimate of the value of a parcel of real estate. This is because there are different types of value related to different appraisal purposes. Some of the possibilities are listed below.

Types of Real Estate Value

- • market
- reproduction
- replacement
- salvage
- plottage
- assessed
- condemned
- reversionary
- appraised
- rental
- leasehold
- insured
- reversionary
- appraised
- rental
- leasehold
- insured
- book value

Market value. Market value is an estimate of the price at which a property will sell at a particular time. This type of value is the one generally sought in appraisals and used in brokers' estimates of value.

Reproduction value. Reproduction value is the value based on the cost of constructing a precise duplicate of the subject property's improvements, assuming current construction costs.

Replacement value. Replacement value is the value based on the cost of constructing a functional equivalent of the subject property's improvements, assuming current construction costs.

Salvage value. Salvage value refers to the nominal value of a property that has reached the end of its economic life. Salvage value is also an estimate of the price at which a structure will sell if it is dismantled and moved.

Plottage value. Plottage value is an estimate of the value that the process of assemblage adds to the combined values of the assembled properties. This concept presupposes that two typc

Assessed value. Assessed value is the value of a property as estimated by a taxing authority as the basis for ad valorem taxation.

Condemned value. Condemned value is the value set by a county or municipal authority for a property which may be taken by eminent domain.

Depreciated value is a value established by subtracting accumulated depreciation from the purchase price of a property.

Reversionary value. Reversionary value is the estimated selling price of a property at some time in the future. This value is used most commonly in a pro-forma investment analysis where, at the end of a holding period, the property is sold and the investor's capital reverts to the investor.

Appraised value. Appraised value is an appraiser's opinion of a property's value. Rental value. Rental value is an estimate of the rental rate a property can command for a specific period of time.
Leasehold value. Leasehold value is an estimate of the market value of a lessee's interest in a property.
Insured value. Insured value is the face amount a casualty or hazard insurance policy will pay in case a property is rendered unusable.
Book value. Book value is the value of the property as carried on the accounts of the owner. The value is generally equal to the acquisition price plus capital improvements minus accumulated depreciation.
Mortgage value. Mortgage value is the value of the property as collateral for a loan.

ESTIMATING VALUE

Principles of Value

III. Principles of Valuation

A. **HIGHEST AND BEST USE -** most profitable use to which a property may be adapted, given legal constraints. (HABU)
B. **SUBSTITUTION -** the value of a property tends to be set by the cost of purchasing an equally desirable and similar property.
C. **SUPPLY AND DEMAND -** the price of a property will increase if the supply decreases and will decrease if the supply increases.
D. **CONFORMITY -** maximum value is realized if the land use conforms to existing neighborhood standards.
E. **INCREASING AND DECREASING RETURNS -** improvements to land and structures produce a proportionate increase in value until some point beyond which the impact of improvements begins to decrease, until improvements cause virtually no change in the property value.
F. **COMPETITION -** high levels of profits attract competitors into an industry; increase in competition results in decreased profits throughout the industry.
G. **CHANGE -** no economic or physical condition remains constant.
H. **CONTRIBUTION -** the value of any component of property consists of what its addition contributes to the value of the whole property.
I. **ANTICIPATION -** value can increase or decrease in anticipation of some future benefit or detriment that will affect the property.
J. **PLOTTAGE -** the principle of combining contiguous property, and, by doing so, increasing the value of the new property. The greater efficiency of land use allows the new value to exceed the combined values of the individual parcels. For example, a strip mall was created from three parcels of vacant land each worth $50,000. After these contiguous properties were combined, the land value became $200,000. The actual process of combining these properties into one is called assemblage.
K. **BALANCE -** is achieved when adding improvements to land and structures will increase the

property value.

L. **REGRESSION -** the principle between dissimilar properties: the worth of the better property
is affected adversely by the presence of the lesser-quality property.

M. **PROGRESSION -** the worth of a lesser property tends to increase if it is located among better properties.

CONFORMITY: Property achieves highest value by being located in harmony with other surrounding property.
For example, a home should be located in a single-family subdivision, not next to an industrial park.

PROGRESSION: A smaller and less expensive dwelling may gain value if it is located near much larger high-priced dwellings.

REGRESSION: A larger and more expensive dwelling may lose value if it is located near smaller low- priced dwellings.

CONTRIBUTION: Value added by one component or part of property as measured to the whole.
For example, how would an extra vacant lot added to a restaurant building as parking affect its value, or how would an added garage affect the value of a home?

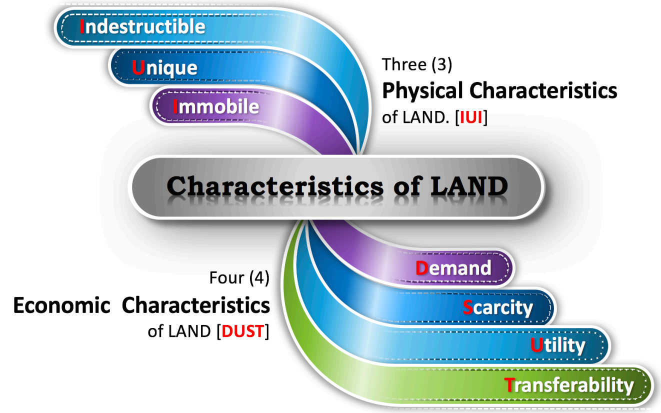
SUBSTITUTION: A theory used to evaluate property that considers the cost of obtaining another comparable property. A buyer will not pay a higher price than what it would cost to purchase another similar property in the same real estate market area.

HIGHEST AND BEST USE: The use of land that produces the highest value, provided that it is legal, economical, and physically possible.

> **For example,** a feasibility study is conducted to determine "**highest and best use**" on a vacant lot zoned commercial located off the expressway exit. The result of the study is that the highest and best use would be a service station accompanied by a coffee shop. The study considers the current or possible future zoning, as well as the market value of the land, cost of improvements, anticipated revenue, etc.

PROPERTY CHARACTERISTICS
PHYSICAL CHARACTERISTICS AFFECTING VALUE

1. **DURABILITY (INDESCRUCTABILITY:**
Although improvements depreciate physically over time, land does not.
Example: Buy some land and let it sit for 30 years and then come back to check on it, it still looks the same. Even a brick building may still look the same. This feature increases the value of real estate.



2. IMMOBILITY: Real estate is not movable.
Example: have you heard that the 3 most important aspect of real estate value is location, location, location. Immobility can be good or bad because if your property is in a good location, that will bring its value upwards. But if it's in a bad location, you cannot move it elsewhere.

3. **HETEROGENEITY (UNIQUE):** (non-homogeneity): Every property is UNIQUE; No two parcels are alike. Even when you have two adjacent lots in the subdivision that would seem to be of the same size and value, they still have two different legal descriptions; one is lot #12
while the other is lot #13.

ECONOMIC CHARACTERISTICS AFFECTING VALUE (D.U.S.T)

1. **DESIRABILITY (DEMAND):** Whether or not there are possible buyers interested in the property that are willing, able, and have the financial means to purchase.
Example: 200-unit condominium complex is built on a waterfront; some units are not facing the water. Chances are that the units facing the water will sell at a higher price because they are more desirable, i.e. there is more —demand on them.

2. **SCARCITY (SUPPLY):** Whether or not there are other similar properties of a comparable nature within the same general area that will compete with the subject property.
Example: a 300-unit condominium complex was pre-sold before construction; finally, one buyer canceled his purchase agreement because he was being transferred out of town. When your buyer wants to make an offer on the last remaining unit, it will be very hard to bargain on the price because of scarcity. Had it been the other way around, for example, if only 50-units were sold and there were 250-units left on the market, there will be some room for bargaining and the price may go down.

3. **UTILITY:** The type of use that the subject property is most suitable for, and whether or not it satisfies the needs of a certain buyer.

Example: a small town known for its large retirement community has a new subdivision being built with mostly one-story Ranch homes. This design will probably prove to be popular with the majority of people in the city, because those of a retirement age may have issues with climbing too many stairs, therefore they will be able to —utilizeǁ this type of design much better than a two storey home, especially with bedrooms located upstairs.

4. **TRANSFERABILITY:** The ability to sell, lease, will property to another person. The more the restrictions on the sale, lease or transfer of property, the less the value.

Example: Property may be the subject of a dispute between partners, or certain action taken by a government entity such as the IRS or DEA, therefore, unless these restrictions are lifted, property will either have a lower value or no value at all.

GROSS RENT / INCOME MULTIPLIER METHOD (BROKER ONLY)

- Mostly suitable for a small income property such as a house, duplex, etc.

Calculating Gross Rent Multiplier (G.R.M.)

Purchase Price	=>	**$280,000**
Monthly Rent (2 Tenants)	=>	**$3,200**
Annual Income (2 Tenants Monthly Rent * 12)	=>	**$38,400**

STEP 1: Formula

Gross Rent Multiplier = $\frac{\text{Purchase Price}}{\text{Annual Income}}$

STEP 2: Substitute Values

Gross Rent Multiplier = $\frac{\$280{,}000}{\$38{,}400}$

STEP 3: Resulting G.R.M.

Gross Rent Multiplier = **7.29 to recover Purchase price**

- **G.R.M.** of 7.29 indicates 7 yrs 4 mo. to recover purchase price.
- **G.R.M**. ranges typically from 4~10
- **G.R.M.** of 12 is considered poor investment and 4 would be good investment opportunity.

- **Gross rent multiplier (GRM)**
  - o G.R.M. Tool calculation allows investors to a quickly (roughly) estimate value of real estate property investment before considering operating expenses and taxes.
  - o Used as a substitute for the income approach in appraising a single-family home. Rule of thumb calculation within Income Capitalization approach.

- o **Formula for GRM: Sales Price ÷ Monthly rental Income = GRM.**
- o **Total Monthly Rental Income × GRM = Estimated Market Value.**

- **Gross income multiplier (GIM)**
  - o Used as a quick way to appraise commercial and industrial properties.
  - o Rule of thumb calculation within the Income Capitalization approach.
  - o **Formula for GIM:** Sales Price ÷ Annual Rental Income = GIM.
- The method applies a multiplier to the estimated gross income of the subject property; the income is either based on the current rent roll of the property or a projection of what the property should earn in a competitive market.
- Although the gross rent/income multiplier provides a fast and brief method of estimating the value, it does not take into consideration any operating expenses, vacancies, etc. therefore it may not be as reliable as the capitalization approach described earlier.

Value = GRM x Rent (Monthly or yearly)

Example: Property #1 was sold for $100,000 and yielded gross ents in the amount of $10,000/yr. What would property #2 be evaluated at with $15,000/yr. in gross rents?

Solution: **G.R.M. = $100,000 / $10,000 = 10 G.R.M for property #1**

10 X $15,000 = $150,000 value for property #2

COMPETITIVE/COMPARATIVE MARKET ANALYSIS - CMA

A. An estimate of property value (conducted usually by the real estate agent) used to assist the seller in determining a listing price for the property by relying on sale and leasing data of comparable properties.

B. A CMA will not be relied upon by the lender in determining the amount of mortgage loan to be provided to the buyer.

C. According to Connecticut state rules/regulations, an real estate licensed salesperson (agent) is authorized to provide the CMA only for the purpose of "***soliciting a listing***" and establishing a selling (or leasing) Listing Agreement agreed "List Price" for a property that the salesperson is preparing to place on the open market via MLS (Multiple Listing Service)

D. **NOTE:** In Connecticut, a salesperson or Broker may charge for a CMA but will be required to refund to charge/cost if the property is sold by that salesperson or Broker/Brokerage.

E. **Methods used for selecting and adjusting comparables** for many residential and some commercial properties are usually similar to those used by licensed appraisers, an agent who faces a complicated valuation task must seek an expert opinion from a licensed appraiser.

Method for Sales Price Adjustments:

- The situations that appraisers most often have to deal with in applying the sales comparison approach are comparables that aren't identical to the subject property. Appraisers go through an adjustment process to compensate for the differences in the properties.
- **Here's a simple example.** The subject property is a three-bedroom, two-bath home. Joan the appraiser doesn't currently know the value of this house. A very similar house sold two months ago for $275,000. The comparable house, called Comparable A*,* is the same in all respects as the subject property except that it has four bedrooms.
- Comparable A is superior to the subject property*.* Joan's research indicates that the value of the fourth bedroom is $25,000. That means that the buyer of Comparable A paid $25,000 more for that house than he or she would have for a three-bedroom house.
- **Joan, when preparing her appraisal report, goes through the process of subtracting that $25,000-bedroom value from the $275,000 sales price of Comparable A. The resulting price of $250,000 is the *adjusted sales price.***
- **$275,000 (sale price of Comparable A) – $25,000 (value of fourth bedroom) = $250,000 (adjusted sales price)**

END

NATIONAL TEST TOPIC #6

APPRAISAL | MARKET VALUATION #6

2020 Practice Classroom Quiz

1. An apartment building grosses $2,000 per month with expenses averaging 35% of gross income. What is the net operating income (NOI) for the project?
   A. $1,300
   B. $24,000
   C. $15,600
   D. $8,400

2. Of the different methods of appraising property, which of the following is the most appropriate for appraising vacant land?
   A. The cost approach
   B. The gross rent multiplier approach
   C. The capitalization approach
   D. Market data (comparison) approach

3. When using the market/sales comparison approach, an appraiser takes the following into consideration:
   A. Income and expenses of property
   B. Capitalization expected by investors
   C. Features that the property has in comparison to other property sold in the neighborhood
   D. Depreciation on improvements

4. Property value is least affected by:
   A. Supply and demand
   B. Quality and features
   C. Activity of buyers in an area
   D. The owner's acquisition cost

5. Which of the following indicates functional obsolescence?
   A. Leak in the roof
   B. Sewage treatment plant next to the property
   C. One-car garage in a neighborhood of mostly two-car garages
   D. High property taxes

6. When a house is located in a neighborhood with several boarded-up houses and gangs on the street, this property loses value due to:

   A. Physical deterioration
   B. Functional obsolescence
   C. Economic obsolescence
   D. Crime effect on occupants

7. When appraising a brand new house surrounded by older houses, the best method used is the:

   A. Income approach
   B. Market comparison approach
   C. Actual cash paid to the builder to erect improvements
   D. Cost approach

8. Which of the following is true about income property evaluation?

   A. The cost of land must be estimated separately and then the cost of improvements must be added to it.
   B. Appraiser must look at acquisition cost when property was purchased.
   C. The capitalization approach is the most suitable.
   D. Expenses such as property taxes, maintenance and insurance are seldom taken into consideration.

9. All of the following are taken into consideration when using the market comparison approach except:

   A. The price of the sold comparables in the neighborhood.
   B. The subject property features such as square footage, number of bathrooms, garage, central air conditioning, etc.
   C. Property location and age in comparison to the sold comparables.
   D. The capitalization rate an investor would reasonably accept.

10. The price that a willing buyer will most probably pay a willing seller under no pressure, and provided that property is available on the market for a reasonable length of time, is known as:

   A. Market price.
   B. Economic price.
   C. Market value.
   D. The buyer's value.

11. A factor which an appraiser multiplies gross income from property by to appraise its value is:

   A. Capitalization factor
   B. Rental factor
   C. Expense factor
   D. Gross rent multiplier

12. In estimating the square footage of a building for replacement purposes, an appraiser would use:
    A. Interior dimensions of the structure.
    B. Lot size dimensions.
    C. Exterior dimensions.
    D. Lot frontage dimensions.

13. To determine the value of a church, the appraiser will probably use:
    A. The income capitalization approach.
    B. The cost approach.
    C. The market data approach.
    D. The congregation approach.

14. A 10,000 sq. ft. mansion surrounded by 1,500 sq. ft. homes would most likely be appraised using:
    A. Market comparison approach
    B. The square foot approach
    C. The cost approach
    D. The gross living area approach

15. When comparing an appraisal report to a comparative market analysis, which of the following is NOT a factor to consider?
    A. An institutional lender will not rely on the market analysis to grant a loan
    B. An appraisal is provided by a state licensed appraiser while the market analysis is provided by a broker.
    C. An appraisal is a determination of value while the market analysis is a recommendation of listing price
    D. An appraisal report is usually more detailed and must follow USPAP

16. The price received for sold property is
    A. Market price
    B. Market value
    C. Arm's length transaction
    D. Appraised price

17. When using the cost approach, an appraiser will consider all of the following factors except:
    A. Economic life
    B. Deferred maintenance
    C. Accrued depreciation
    D. NOI

18. All of the following are considered principles of value except:
    A. Conformity
    B. Substitution
    C. Contribution
    D. Acquisition cost

19. When a sale occurs in a competitive market and under no duress, this transaction is known as:
   A. Fair market value transaction
   B. Arm's length transaction
   C. Highest and best value
   D. Full anticipation transaction

20. Which of the following would have the least effect on property value?
   A. Interest rates
   B. Economic growth
   C. Brokers' commissions
   D. Loan availability

ANSWERS- **VALUATION & MARKET ANALYSIS**

1. C
2. D
3. C
4. D
5. C
6. C
7. D
8. C
9. D
10. C
11. D
12. C
13. B
14. C
15. C
16. A
17. D
18. D
19. B
20. C

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TOPIC 7

Financing

EXAM TOPIC AREAS

A. **Basic concepts and terminology**
   1. Points
   2. LTV
   3. PMI
   4. Interest
   5. PITI
   6. Financing instruments (mortgage, promissory note, etc.)

B. **Types of loans**
   1. Conventional loans
   2. FHA Insured loans
   3. VA guaranteed loans
   4. USDA/rural loan programs
   5. Amortized loans
   6. Adjustable-rate mortgage loans
   7. Bridge loans
   8. Owner financing (installment and land contract/contract for deed)

C. **Financing and lending**
   1. Lending process application through closing
   2. Financing and credit laws and rules
      a. Truth in lending
      b. RESPA
      c. Equal Credit Opportunity
      d. CFPB/TRID rules on financing and risky loan features
   3. Underwriting
      a. Debt ratios
      b. Credit scoring
      c. Credit history

STUDY NOTES:

I. Introduction to the Real Estate Financing Market

A. **Federal Reserve System**

1. Created to help maintain sound credit conditions
2. Helps counteract inflationary and deflationary trends
3. Attempts to create a favorable economic climate
4. Divides country into 12 Federal Reserve districts
5. Regulates the flow of money and interest rates
    a. Controls bank reserve requirements
    b. Controls bank discount rates

I. Theories of Mortgage Law

A. **Lien theory** - the mortgage is viewed as a lien on real property in many states.
B. **Title theory** - the lender is viewed as the conditional owner of mortgaged land in some states.
C. **Intermediate theory** - a number of states allow the lender to take possession of the mortgaged real estate on default.

II. Mortgage Loan

A. **Mortgage origination** - the lending institution that originally qualifies the borrower, orders the appraisal, initiates the Uniform Residential Loan Application (FNMA 1003), and charges a loan origination fee.
B. **Mortgage** - a document by which the mortgagor (borrower) places a lien on the property in favor of the mortgagee (lender) as security for debt.
C. **Note -** promise to repay debt; a negotiable instrument.

III. Trust Deed - Three-Party Instrument Used in Place of a Mortgage in Some Areas of the Country

A. Conveys real estate as security for loan to a third party, the trustee
B. Trustee holds the title on behalf of the lender, known as the beneficiary; the trustee is the legal owner, and the beneficiary is the holder of the note; the borrower retains the equitable title to the property, and the deed of the trust becomes the lien against it
C. The trustee may commence a foreclosure action if the borrower (trustor) defaults; a reconveyance deed returns title to trustor when trust deed has been paid in full.

IV. Types of Loans

A. **Amortized loan, or fixed payment** - equal monthly payments credited first to interest due, then applied to the loan balance.
B. **Graduated payment mortgage** - allows for smaller payments in the early years and increased payments in the later years. Causes negative amortization by adding the early years of deferred interest to principle.
C. **Straight or interest-only loan** - allows for payments of interest only with a lump-sum payment of principal at maturity.
D. **Balloon payment** - payments of principal and interest are paid to the lender over a relatively short period; the outstanding principal balance is due in a lump sum at a predetermined future date (partially amortized loan payment plan).
E. **Subprime loans** - loans to borrowers with a weakened credit history who have a greater likelihood of default. The lender compensates for the greater risk by charging higher fees and interest rates than those on traditional loans.

V. Mortgage Provisions

A. **Acceleration clause** - if the borrower defaults, the lender has the right to declare the entire debt due and payable.
B. **Assignmen -** the mortgagee becomes the assignor and executes assignment to the assignee, who becomes the new owner of the mortgage and debt.
C. **Defeasance clause** - the mortgagee is required to execute the release or satisfaction of the mortgage when the note is fully paid.
D. **Alienation (due-on-sale) clause** - if the borrower sells the property, the lender has the choice of either declaring the entire debt due and payable or allowing the buyer to assume the loan.
E. **Buying "subject to" versus assuming** - if the property is sold "subject to" the mortgage, the buyer is not personally liable to pay the entire debt (the seller remains liable); if the buyer assumes the mortgage, he or she becomes personally liable for payment of the entire debt. The seller is secondarily liable.
F. **Subordination agreements** - a subordination clause is one that grants or permits a subsequent mortgagor to take priority in lien structure.

VI. Mortgage Foreclosure and Redemption

A. **Judicial foreclosure**
  1. Lender sues the borrower in court; obtains judgment and court order to sell.
  2. Property sold at public sale to the highest bidder.

B. **Nonjudicial foreclosure**
  1. The mortgage generally must include a power-of-sale clause.
  2. A notice of default must be recorded and a public sale advertised in the newspaper.
  3. The property is sold at a public sale to highest bidder.

C. **Strict foreclosure** - the court may award title to the lender.
D. **Deed in lieu of foreclosure** - mortgagor gives deed to mortgagee when mortgagor is in default under terms of mortgage; this allows mortgagor to avoid foreclosure.
E. **Short sale** - a procedure to prevent foreclosure that a bank uses in an effort to minimize the financial loss that would be involved in foreclosing. Lenders negotiate with lienholders for a payoff that is less than they are owed, or for the sale of real estate for an amount that is less than the full amount of the debt.
F. **Redemption** - process by which the borrower regains interest in the property.
  1. **Equitable redemption**
    a. Occurs prior to public sale.
    b. If the borrower pays the amount due plus the costs prior to the public sale, the mortgage is reinstated.
    c. If not redeemed, the property is sold at a public sale to the highest bidder.
  2. **Statutory redemption**
    a. Occurs after public sales in some states and continues for a period of time specified by law.
    b. The borrower may pay to the foreclosure purchaser the sale price in full plus costs.

G. **Deficiency judgment** - f the property is old and he proceeds re nsufficient to pay the mortgage and foreclosure costs, the difference is a deficiency; the lender usually can sue the original borrower for the difference (process of deficiency judgment).

VII. Types of Mortgages

A. **Conventional**

1. Payment of the debt based solely on the borrower's ability to pay, with security provided by the mortgage; neither insured nor guaranteed by government agency.
2. Lender sets the terms subject to many of the rules established by the secondary mortgage market. Loans originated by some institutions are sold to investors in the secondary market. Other institutions keep the loans they make; these are called portfolio loans.
3. **Loan-to-value ratio (LTVR)** depends on the borrower's credit risk and/or size of the down payment. For example, if a borrower put down 10 percent of a $200,000 home, then the **LTV** ratio would be 180,000 (200,000–20,000) divided by 200,000, or 90 percent.
4. If the loan-to-value ratio exceeds a given level, 80 percent for example, the lender may require private mortgage insurance (PMI).
5. Internet lenders provide borrowers with another viable origination option. However, online lending can be tricky, and some counseling should be sought before borrowing mortgage money online.

B. **Federal Housing Administration (FHA) insured**

1. FHA insures approved lenders against loss on loans made on real property.
2. Interest rates float with the open market.
3. The borrower finances an up-front FHA insurance premium of 1.50 percent (which may be partially refundable); borrower then pays a monthly (nonfinanceable) insurance premium (MIP) based on ½ percent of the mortgage amount.
4. Mortgaged property must be appraised by an FHA-approved appraiser.
5. FHA does not allow a prepayment penalty.
6. FHA mortgages are assumable with qualification.
7. Discount points are generally used to reduce the interest rate
8. (1 point = 1 percent of the loan balance); these are generally negotiated between the seller and the buyer.

C. **Department of Veterans Affairs guaranteed (DVA loans)**

1. DVA does not allow a prepayment penalty.
2. A DVA loan may be assumed by a qualified nonveteran.
3. DVA guarantees home loans for eligible veterans or eligible dependents with little or no down payment.
4. The interest rate is set by the market.
5. DVA does not charge the borrower for the guarantee; however, the borrower must pay up to a 3.5 percent funding fee to the DVA, on any no-down-payment loan, in addition to any other fees.
6. Mortgaged property must be appraised by a DVA-approved appraiser.
7. DVA sets a limitation on the loan amount of four times the amount of the veteran's entitlement guarantee.
8. DVA guarantees the lender up to $60,000 of the loan balance.
   A. Most investors are comfortable purchasing a loan four times that amount (4 × 60,000 = $240,000) made to a qualified veteran.
9. Discount points generally are negotiated between the seller and the buyer.
10. In some cases, the DVA will make direct loans to eligible veterans or their dependents.
11. DVA requires appraisers to complete a Certificate of Reasonable Value (CRV); the DVA guarantee is based on either the amount of the CRV or the selling price, whichever is less.
12. National Guard members and reservists with at least six years of service now are eligible for DVA-guaranteed loans.

D. **Rural Development and Farm Agency (formerly Farmers Home Administration)**

1. Rural Development makes and guarantees housing loans to people with low incomes in rural areas in communities of 10,000 population or less.
2. Farm Service Agency makes and guarantees loans to farmers and ranchers.

E. **Rural Economic and Community Development services,** makes, and guarantees loans to homeowners in rural areas.

F. **Privately insured**

1. Depending on the buyer's credit score, the buyer may obtain a conventional loan for up to 103 percent of the property's appraised value.
2. The buyer is charged the market rate of interest plus reasonable insurance premium costs.
3. The borrower's insurance protects the lender against loss on the upper 20 to 25 percent portion of the loan.
4. PMI insurance premiums are made a part of the borrower's monthly payments.
5. As property values rise and the loan-to-value ratio becomes 80 percent or less, the PMI insurance may be dropped.
    a. Requires either the lender's or investor's approval and generally a new appraisal
    b. Insurance must generally be held for two years, and the mortgagor must have a 20 percent equity to request that the insurance be dropped; when the mortgagor's equity position reaches 22 percent, the lender is required to drop the insurance.

H. **Purchase-money mortgage** - given by the buyer to the seller as part of the purchase price (owner financing); legal title passes to the buyer.

I. **Blanket mortgage** - covers more than one property or lot; generally includes a partial-release clause.

J. **Package mortgage** - includes real estate and (expressly) all fixtures and appliances located on the property.

K. **Open-end mortgage**

1. Secures the note executed by the borrower to the lender and any future advances of funds by the lender to the borrower.
2. Terms usually restrict an increase in debt to a limit of either the original debt or a specified amount in the mortgage.
3. Additional loan amounts are figured at prevailing interest rates.

L. **Construction loans**

1. Generally short-term or interim loan to finance construction of an improvement.
2. Periodic payments or draws made by the lender to the owner for work completed since the previous payment.

M. **Wraparound mortgage** (all-inclusive second deed of trust)

1. Allows the borrower who is paying an existing mortgage to obtain additional financing from a second lender.
2. New lender agrees to keep up payments on the existing loan; gives the borrower a new, increased loan at a higher interest rate.
3. The new lender makes payments on the original loan; the borrower makes payments to the new lender on the larger loan in an increased amount.

N. Graduated-payment mortgage - only used during times of high interest rates.

1. Initial payments are low but increase over the life of the loan.
2. Allows the buyer to purchase a home with monthly payments lower than those on a level payment.
3. Aimed at helping first-time buyers who have increasing income potential.

O. **Adjustable-rate mortgage (ARM)**

1. Contains interest-rate provision related to a selected index.
2. The interest rate may be adjusted periodically (either up or down). A margin is added to the index to determine the interest rate.
3. ARMs can be converted to fixed-rate mortgages (FRMs). They are fixed for either 5 or 7 years and then are annually adjusted.

P. **Reverse annuity mortgage (RAM)**

1. A Home Equity Conversion Mortgage for borrowers; must be 62 years of age or older to qualify for the loan.
2. The note becomes due on a specific date, at the sale of the property, or at the death of the borrower.

Q. Participation mortgage - lender receives interest and an equity position in a project, known as equity kicker, or a percentage of the income of the property.

R. **Buydowns**

1. **Temporary** - To help the borrower qualify for a loan, the seller agrees to subsidize the buyer's PI payment. For example, if the interest rate is 7% and the seller agreed to help finance a 2 – 1 buy-down loan, then the borrower would make an initial payment based on a 5% interest rate the first year and 6% the second year. The seller would subsidize the buyers' PI payment 2% the first year (7% – 2% = 5%) and 1% the second year (7% – 1% = 6%). In the third year the temporary subsidy goes away and the buyer's payment is based on a 7% interest rate.
2. **Permanent** - In order for the borrower to qualify for a larger than usual loan, discount points can be paid at closing to permanently buy down the existing interest rate. For example, if a borrower qualified to make an $1,100 PI payment, amortized over 30 years at 5.50% ($5.68 per $1,000), then the amount   ortgaged would be ($1,100 divided by 5.68) $193,662. However, if the sellers paid enough discount points to permanently buy down the interest rate to 5.00% (instead of 5.50%), then the amount mortgaged would be increased to ($1,100 divided by 5.37) $204,842.

VIII. The Money Market

A. **General characteristics**

1. Money may be viewed as a means of payment, storehouse of purchasing power, standard of value.
2. Money market is regulated by the federal government through the Federal Reserve System and the U.S. Treasury.

B. **Federal Reserve System (Fed)**

1. Regulates the flow of money through member banks by controlling reserve requirements and discount rates.
2. Tempers the economy through open-market operations.

C. **U.S. Treasury**

1. In effect, our nation's fiscal manager.
2. Responsible for supervising the daily fiscal borrowing and spending operations of the federal government.

IX. Sources of Real Estate Financing

A. **Savings and loan associations**

1. Principal function: to promote thrift and home ownership.
2. Regulated on the national level by the Office of Thrift Supervision.
3. Deposits are insured by the Savings Association Insurance Fund (SAIF) for up to

$100,000 per depositor; SAIF is part of the FDIC.
4. Local in nature

B. **Commercial banks**
1. Prefer short-term loans but have been significant participants in residential mortgage lending.
2. Deposits are insured by the Bank Insurance Fund (BIF) for up to $100,000 per depositor; BIF is part of the FDIC.

C. **Mutual savings banks**
1. Primarily savings institutions in the northeastern United States.
2. Active in mortgage market.
3. Prefer FHA and DVA loans.

D. **Life insurance companies**
1. Prefer long-term commercial, industrial loans.
2. Seek equity position in projects financed.
3. Regulated by state law.

E. **Mortgage banking companies**
1. Originate loans with their own money and money belonging to other institutions and from other sources (pension funds, private individuals).
2. Service loans they originate.

F. **Mortgage brokers** - originate loans for other lenders but do not service loans.

G. **Sale of state mortgage bonds**
1. Authorized by federal government.
2. Lower interest rates are usually charged to low-income and moderate-income buyers.
3. Usually for first-time buyers only.

H. **Owner assisted**
1. Contract for deed, land contract.
2. Take back second mortgage.

X. Secondary Mortgage Market

A. Market in which loans are bought and sold after they have been originated and funded.B. **Warehousing agencies** play a major role in the secondary market by purchasing a number of mortgage loans and assembling them into packages for resale to investors.

C. **Major warehousing agencies**
1. **Federal National Mortgage Association (FNMA) -** Fannie Mae
   a. Publicly traded corporation authorized to purchase conventional as well as FHA and DVA loans.
   b. Raises funds to purchase loans by selling government-guaranteed FNMA bonds at market interest rates.
2. **Government National Mortgage Association (GNMA) -** Ginnie Mae
   a. Federal agency designed to administer a special assistance program and to work with the FNMA in secondary market activities.
   b. Can join forces with the FNMA in times of tight money and high interest rates; through a tandem plan, the FNMA can purchase high-risk, low-yield loans at full market rates, while the GNMA guarantees payment and absorbs the difference between low-yield and current market prices.
   c. Government agency authorized to purchase government-insured FHA mortgages; government-guaranteed VA mortgages; and government-subsidized Rural Development Mortgages from intermediaries in the secondary mortgage market.
3. **Federal Home Loan Mortgage Corporation (FHLMC) -** Freddie Mac
   a. Government-chartered corporation created to provide secondary mortgage market for conventional loans.
   b. Has the authority to purchase conventional, FHA, and DVA mortgages;

pool them; and sell bonds in the open market with mortgages as security.

XI. Mortgage Fraud

A. **Fraud perpetrated through acts such as the use of identity theft and false documents**, and the occasional willing or unwilling assistance of professionals in real estate. Examples include the following.

1. **Fictitious or stolen identity** - false identity is used on a loan application without the true person's knowledge.
2. **Inflated appraisals** - an appraiser works in collusion with a borrower or a lender to provide a misleading appraisal report to the lender by inaccurately stating an inflated property value.

B. **Mortgage fraud is investigated by the FBI and is punishable by up to 30 years in federal prison, a $1 million fine, or both.**

XII. Property Insurance

A. **Required to obtain mortgage;** figured annually and often budgeted monthly.
B. **Various types of polices like renters insurance (HO-4),** homeowners insurance (HO-2 or HO-3), and condominium insurance (HO-6) for interior surfaces.
C. **CLUE (claim activity and property damage)** reports are ordered by most insurance companies on property being purchased. (CLUE is an acronym for Comprehensive Loss Underwriting Exchange). Insurers use the report to ascertain patterns of possible future claims and adjust their insurance premiums according to risk.

XIII. Closing Statements (settlement statement or adjustment sheet)

A. Related to the completion of the real estate transaction, when the seller delivers title to the buyer in exchange for payment of the purchase price by the buyer.
B. Detailed accounting of real estate transaction; shows all funds received, all charges and credits made, all funds paid out.
C. Prepared by the broker, escrow office, attorney, or any other person designated to process the details of the sale.
D. Indicates how all closing costs plus prepaid and unpaid property expenses are allocated between the buyer and the seller.
E. Closing statement procedures generally reflect local custom as well as state and federal laws (for example, RESPA).

XIV. Other Important Terms

A. **Amortized mortgage (direct-reduction loans) -** regular monthly payments, applied first to the interest, with the balance to the principal, over the term of the loan.
B. **Balloon payment** - final payment of the loan; larger than previous payments and repays the debt in full.
C. **Equity** - value of the owner's interest in the property; the difference between the value of the property and all the liens on the property.
D. **Subordination agreement** - changes the order or priority of the liens between two creditors.
E. **Usury** - charging a rate of interest in excess of the maximum rate allowed by state law.
F. **Seller financing** - the seller of the real estate provides financing for the sale by taking back a secured note in the form of a purchase-money mortgage, land contract, or deed of trust.
G. **Disintermediation** - lenders experience a rapid withdrawal of funds into alternative investments which weakens the lender's position in the money market.

H. **Arbitrage -** profitable difference between interest rates in financing arrangements such as wraparound mortgages.

I. **Hypothecation** - pledging property as security for the loan without losing possession of it.

J. **Impound account -** trust account created to set aside funds for the future needs of a property, for example, to provide funds for the payment of real estate taxes and renewal premiums for insurance.

K. **Discount points** - money expressed in the form of a percentage. A point equals one percent of the loan amount. For example, if two discount points were paid on a $200,000 loan, the amount would be $200,000 × 2% or $4,000. Often the seller is asked to pay a discount point or two in order to help the buyer obtain financing.

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NATIONAL TEST TOPIC #7

FINANCING – PART 1 #7A

2020 Practice Classroom Quiz 7A

1. If a property sold at a mortgage foreclosure does not bring an amount sufficient to satisfy the outstanding mortgage debt, the mortgagor may be responsible for
A) a default judgment.
B) a deficiency judgment.
C) liquidated damages.
D) punitive damages.

2. In absence of an agreement to the contrary, the mortgage having priority will be the one
A) for the highest amount.
B) that was recorded first.
C) that was signed first.
D) that is a construction loan.

3. When real estate is sold under an installment land contract and the buyer takes possession of the property, the legal title
A) is subject to a purchase-money mortgage.
B) must be transferred to a land trust.
C) is kept by the seller until the purchase price is paid according to the contract.
D) is transferred to the buyer.

4. Mortgage lenders want assurance that future real estate taxes will be paid. The most common way to do this is to require the borrower to
A) obtain title insurance.
B) sign a note.
C) pay into an impound account.
D) submit paid tax receipts.

5. The seller agrees to sell the house to the buyer for $100,000. The buyer was unable to qualify for a mortgage loan for this amount so the seller and the buyer enter into a contract for deed. The interest the buyer has in the property under a contract for deed is
A) legal title.
B) equitable title.
C) joint title.
D) mortgagee in possession.

6. The mortgagee foreclosed on a property after the borrower defaulted on the loan payments. At the foreclosure sale, however, the house sold for only $129,000. The unpaid balance of the loan at the time of the sale was $140,000. What must the lender do to recover the $11,000 the borrower still owes?

A) Sue for damages
B) Sue for specific performance
C) Seek a judgment by default
D) Seek a deficiency judgment

7. The purpose of a mortgage is to

A) provide security for a loan.
B) convey title of the property to a lender.
C) restrict the borrower's use of the property.
D) create a lien on the property.

8. If a buyer obtains a $50,000 mortgage with four points, how much will the lender charge at closing?

A) $6,000
B) $200
C) $2,000
D) $40,000

9. The pledging of property as security for payment of a loan without surrendering possession is

A) disintermediation.
B) equity.
C) hypothecation.
D) subordination.

10. A "friendly foreclosure" enables a mortgagor to prevent the mortgagee from taking the property by statutory means. This can be accomplished by use of a(n)

A) deed in lieu of foreclosure.
B) reconveyance deed.
C) assumption.
D) escrow deed.

11. The defeasance clause in a mortgage requires the mortgagee to execute a(n)

A) assignment of mortgage.
B) satisfaction of mortgage.
C) subordination agreement.
D) partial release agreement.

12. All the following clauses in a loan agreement enable the lender to demand the entire remaining debt be paid immediately *EXCEPT* a(n)

A) due-on-sale clause.
B) defeasance clause.
C) acceleration clause.
D) alienation clause.

13. **When a mortgage loan has been paid in full, it is important for the borrower to be sure that**
    A) the paid note is placed in a safe deposit box.
    B) he or she obtains a deed of partial reconveyance.
    C) the paid mortgage is returned to the lender.
    D) a satisfaction of mortgage is recorded.

14. **The clause in a trust deed or mortgage that permits the lender to declare the entire unpaid balance immediately due and payable upon default is the**
    A) judgment clause.
    B) escalator clause.
    C) forfeiture clause.
    D) acceleration clause.

15. **An existing mortgage loan can have its lien priority lowered through the use of a**
    A) hypothecation agreement.
    B) satisfaction of mortgage.
    C) subordination agreement.
    D) reconveyance of mortgage.

16. **The fee charged by a mortgage broker to arrange a loan is a(n)**
    A) prepayment penalty.
    B) advance interest payment.
    C) loan origination fee.
    D) prepayment of mortgage insurance.

17. **A promissory note**
    A) may not be executed in connection with a real estate loan.
    B) is an agreement to perform or not to perform certain acts.
    C) makes the borrower personally liable for the debt.
    D) is a guarantee by a government agency.

18. **Charging more interest than is legally allowed is known as**
    A) escheat.
    B) usury.
    C) a deficiency.
    D) an estoppel.

19. **In what way does a deed of trust differ from a mortgage?**
    A) Number of parties involved in the loan
    B) Obligation of the borrower to repay the funds
    C) Redemption rights allowed after foreclosure
    D) Time period permitted to cure a default

20. **The right a mortgagor has to regain the property by paying the debt after a foreclosure sale is called**
    A) acceleration.
    B) redemption.
    C) reversion.
    D) recapture.

21. A woman has just made the final payment on her home mortgage to her lender. There will still be a lien on her property until the lender records a(n)
A) satisfaction of mortgage.
B) reconveyance of mortgage.
C) alienation of mortgage.
D) reversion of mortgage.

22. A land contract provides for the
A) sale of unimproved land only.
B) sale of real property under an option agreement.
C) conveyance of legal title at a future date.
D) immediate transfer of reversionary rights.

23. A mortgagor is the one who
A) gives a mortgage.
B) holds a mortgage.
C) provides mortgage funds.
D) forecloses on a mortgage.

24. Under an installment contract, the title to the property is held by the
A) vendor.
B) vendee.
C) trustor.
D) trustee.

Answer Key – FINANCING PART ONE-1 2020

1. B
2. B
3. C
4. C
5. B
6. D
7. A
8. C
9. C
10. A
11. B
12. B
13. D
14. D
15. C
16. C
17. C
18. B
19. A
20. B
21. A
22. C
23. A
24. A

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NATIONAL TEST TOPIC #7

FINANCING – PART 2 #7B

2020 Practice Classroom Quiz 7B

1. A woman has owned her house for over 50 years. It has fallen into disrepair, but because she lives on a fixed income she does not have the money to make the needed repairs. She has a considerable amount of equity in the house. What type of loan best suits her needs?
A) Home equity loan
B) Reverse mortgage
C) Blanket loan
D) Open-end loan

2. A man is selling his property for $225,000. He has a loan balance of $50,000. He has agreed to provide financing to the purchasers in the amount of $200,000 and will continue to make payments on the original loan. This type of loan is called a
A) package loan.
B) wraparound loan.
C) blanket loan.
D) loan assumption.

3. The type of mortgage loan that uses both real and personal property as security is a
A) blanket loan.
B) package loan.
C) purchase-money mortgage.
D) wraparound loan.

4. A lender will take certain factors into consideration when deciding whether to grant a borrower a mortgage loan. Which of the following is a violation of the Equal Credit Opportunity Act (ECOA)?
A) Marital status of the borrower
B) Creditworthiness of the borrower
C) Amount of the borrower's income
D) Ability of the borrower to make the payments

5. Which of the following would be considered a trigger item under Regulation Z?
A) "Low monthly payments"
B) "FHA financing available"
C) "A steal at only $175,000!"
D) "Only $10,000 down"

6. PMI is the acronym for private mortgage insurance, which is often used by borrowers whose LTV (loan-to-value ratio) is less than 20 percent. Lenders must cease charging PMI when the LTV reaches

A) 22 percent.
B) 27 percent.
C) 29 percent.
D) 35 percent.

7. An extension of credit from a seller to a buyer to allow the buyer to complete the transaction is called a

A) growing-equity mortgage.
B) purchase-money mortgage.
C) package mortgage.
D) blanket mortgage.

8. The principal distinction between the primary mortgage market and the secondary mortgage market is in the

A) insuring versus the guaranteeing of mortgage loans.
B) origination versus the purchase of mortgage loans.
C) use of mortgages versus the use of deeds of trust.
D) use of discount points versus the use of origination fees.

9. A type of long-term financing that has become popular because initial payments are lower due to no principal being paid is called a(n)

A) amortized loan.
B) balloon loan.
C) package loan.
D) interest-only loan.

10. The availability of funds for real estate mortgage loans is affected by the Federal Reserve System through which of the following?

A) Discount rates
B) Federal National Mortgage Association
C) Federal Housing Administration
D) Resolution Trust Corporation

11. Freddie Mac

A) operates mostly in the primary mortgage market.
B) operates mostly in the secondary mortgage market.
C) guarantees payment of Freddie Mac mortgages.
D) buys mostly FHA loans.

12. A subdivider had a mortgage loan on his entire housing subdivision. When he sold a lot to a buyer, he was able to deliver title to that lot free of the mortgage lien by obtaining a partial release. What type of loan did the developer have?

A) Blanket mortgage
B) Purchase-money mortgage
C) Package mortgage
D) Open-end mortgage

13. When compared with a 30-year payment period, taking out a loan with a 20-year payment period would result in

A) slower equity buildup.
B) greater impound requirements.
C) lower monthly payments.
D) higher monthly payments.

14. A real estate loan payable in periodic installments that are sufficient to pay the principal in full during the term of the loan is called a

A) conventional loan.
B) straight loan.
C) partially amortized loan.
D) fully amortized loan.

15. Which statement is *TRUE* about VA-guaranteed mortgages?

A) Discount points must be paid by the seller.
B) The borrower may have a prepayment penalty clause in the loan.
C) Funding fee amounts are negotiable.
D) The borrower must apply for a certificate of eligibility.

16. A mortgage broker generally offers which of the following services?

A) Handling the escrow procedures
B) Bringing the borrower and the lender together
C) Providing credit qualification and evaluation reports
D) Granting real estate loans using investor funds

17. An FHA-insured mortgage loan would be obtained from which of the following?

A) The Federal Housing Administration
B) The Department of Housing and Urban Development
C) Any FHA-approved lending institution
D) Any FHA-approved insuring institution

18. A woman's son will start college soon. She has lived in her home for ten years. What financing option would be preferable for the woman to obtain funds to pay for her son's schooling?

A) Participation financing
B) Open-end loan
C) Wraparound loan
D) Home equity loan

19. Which pair of terms is synonymous?

A) Interim financing and construction loan
B) Construction loan and pass-through loan
C) Pass-through loan and takeout loan
D) Takeout loan and construction loan

20. Fannie Mae

A) makes FHA loans.
B) buys FHA loans.
C) services FHA loans.
D) insures FHA loans.

21. A borrower obtained a $7,000 second mortgage loan for five years at 6 percent interest per annum. Monthly payments of principal and interest were $50. The final payment included the remaining outstanding principal balance. What type of loan is this?
A) Fully amortized loan
B) Straight loan
C) Partially amortized loan
D) Accelerated loan

22. Fannie Mae, Ginnie Mae, and Freddie Mac all
A) originate residential mortgage loans.
B) purchase existing mortgage loans.
C) insure residential mortgage loans.
D) guarantee existing mortgage loans.

23. All of the following loans to individuals are affected by the truth-in-lending law under Regulation Z *EXCEPT*
A) household use.
B) business use.
C) room additions.
D) swimming pools.

24. The type of real estate loan that allows the lender to increase the outstanding balance of a loan up to the original sum in the note while advancing additional funds is the
A) wraparound mortgage.
B) open-end mortgage.
C) growing-equity mortgage.
D) graduated-payment mortgage.

25. The grantor becomes the lessee and the grantee becomes the lessor under which of the following financing arrangements?
A) Partial sale
B) Wraparound mortgage
C) Sale and leaseback
D) Assumption of mortgage

26. A man has been making periodic payments of principal and interest on a loan, but the final payment will be larger than the others. This is a(n)
A) balloon payment loan.
B) fully amortized loan.
C) FHA loan.
D) straight loan.

Answer Key – **FINANCING PART TWO-1 2020**

1. B
2. B
3. B
4. A
5. D
6. A
7. B
8. B
9. D
10. A
11. B
12. A
13. D
14. D
15. D
16. B
17. C
18. D
19. A
20. B
21. C
22. B
23. B
24. B
25. C
26. A

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TOPIC 8

Land Use Controls & Regulations

EXAM TOPICS

A. Government rights in land
1. Property taxes and special assessments
2. Eminent domain, condemnation, escheat

B. Government controls
1. Zoning and master plans
2. Building codes
3. Regulation of special land types
   a. Flood zones
   b. Wet lands
4. Regulation of environmental hazards
   a. Types of hazards
   b. Abatement and mitigation
   c. Restrictions on contaminated property

C. Private controls
1. Deed conditions or restrictions
2. Covenants, conditions, and restrictions (CC&Rs)
3. Homeowners association regulations

STUDY NOTES:

I. Local, State, and Federal Government Land Rights (PETE)

A. **Police power** - power of the state to promulgate laws aimed at promoting the general welfare and protecting public health and safety; examples of the use of police power include zoning, building codes, environmental protection; enabling acts are created by states to grant zoning power to municipal governments.

B. **Taxation** - power to tax real estate to meet the public needs of the government.

C. **Eminent Domain** - power of the government to acquire private property for public use while providing just compensation (condemnation) for the property owner.

D. **Escheat** - state laws that provide for ownership of real estate to revert to the state when the owner dies intestate and leaves no heirs or when the property is abandoned.

E. **Water rights** - ownership of water and land adjacent to it as determined by state law, which is based on either the doctrines of riparian and littoral rights or on the doctrine of prior appropriation; owners generally have the right to use water so long as they do not pollute or interrupt the flow.

1. **Riparian rights** - rights granted to owners along a nonnavigable river or stream.
2. **Littoral rights** - rights granted to owners along an ocean or large lake.
3. **Doctrine of Prior appropriation** - the right to use water is controlled by the state rather than by the adjacent landowner. A person must show a beneficial use for the water, such as crop irrigation, in order to secure water rights.

II. Control of Land Use

A. **Public land-use controls** - under police power, each state has the authority to adjust regulations required for protecting public health, safety, and the general welfare.

1. **Zoning** - zoning laws are local laws that regulate and control the use of land in the community, generally pertaining to the height, bulk, and use of the buildings. Powers to zone are conferred on municipal governments by state enabling acts.
    - a. **Nonconforming use** - use in existence prior to the passage of a zoning ordinance and allowed to continue even though it does not conform
        - (1) If property that exists as nonconforming is destroyed, it cannot be rebuilt without the approval of the zoning authority.
    - b. **Variance** - approval by a zoning authority that allows an individual to deviate from the zoning requirement.
    - c. **Conditional use permit** - allows for a use that does not conform with existing zoning but is necessary for the common good, such as locating a medical clinic in a primarily residential neighborhood.
    - d. **Downzoning** - land zoned for residential or commercial use is rezoned for conservation only; it also applies to changes from dense to less-dense usage. The state generally is not responsible for compensating property owners for any loss of value unless the court finds that a "taking" of value has occurred, such as land being rezoned from residential to conservancy.
    - e. **Buffer zone** - a land area that separates one land use from another; a park that separates a residential neighborhood from a shopping center.
    - f. **Spot zoning** - reclassification of a small area of land for use that does not conform to the zoning of the rest of the area.
    - g. **Planned unit development (PUD)** - planned mix of diverse land uses such as housing and recreation in one comprehensive plan.
    - h. **Density zoning** - ordinances that restrict the average maximum number of houses per acre that may be built within a particular area. As communities expand, urban sprawl becomes a concern because extensive community growth often leads to issues involving traffic congestion, overcrowding of schools, and loss of open space.
2. **Building codes** - ordinances that specify standards for construction, maintenance, and demolition.
3. **City plan specifications** - a master plan to guide physical development of a community.
4. **Subdivision regulations** - apply to the location of streets, minimum lot size, etc.
5. **Environmental protection laws**
    - a. **Federal** - the National Pollutant Discharge Elimination System (NPDES), for example.
    - b. **State** - Connecticut has passed its' own environmental legislation.

B. **Private land-use controls - restrictions** specified by the owner in the deed when conveying the property.

C. If conflict exists between a zoning ordinance and a deed restriction, the more Restrictive of the two takes precedence.

D. **Taxation on real estate**

1. **Real estate taxes generally take priority** over other liens; may be enforced by the

court sale of real estate that is free of other liens.

2. **Ad valorem tax** (Latin for "according to the value") - includes taxes levied on real estate by various governmental units and municipalities.
3. **Assessment -** appraisal of value for tax purposes by an assessor representing the municipality in which the property is located.
4. **Equalization factor** - used in some states to correct general inequalities in statewide tax assessment.
5. **Computation of tax rate**
    a. The taxing district adopts a budget that identifies the amount of income to be raised from real estate taxes.
    b. To arrive at the tax rate, divide the amount of money required for the budget by the total assessed value of all properties within the taxing district. For example, if the taxing district must raise $600,000 from real estate taxes and the total assessed value is $10,000,000, the tax rate would be $600,000 ÷ $10,000,000 = 0.06, or 6 percent.
    c. The tax rate may be expressed in mills. For example, 40 mills = 4% of the taxable value; 45 mills = 4.5% of the taxable value.
    d. The tax bill for a property is calculated by applying the tax rate to the taxable value of the property; for example, a home assessed for tax purposes at $200,000 and using a tax district rate of 45 mills, or 4.5% of the taxable value, would be required (annually) to pay $9,000. Divided by 12, the monthly tax obligation would be $750.
6. **Special assessments -** special taxes levied on real estate; require property owners to pay for improvements that specifically benefit their real estate (installation of a curb and gutter, streets, water system, sewers, etc.).
7. **Condominium associations -** these entities have the legal right to assess their property owners for common area maintenance (CAM) dues as well as special assessments.

III. Floodplain, Wetlands, and Shoreline Regulations

A. **Floodplain** - portions of land located near running bodies of water, such as rivers or lakes, that are subject to flooding; government controls generally restrict building in a floodplain.

B. **Wetlands** - areas of land where groundwater is close to or at the surface of the ground for a period of time each year that may produce swamps, floodplains, or marshes; because these areas of land are prone to flooding, they are covered by various federal, state, and local controls, such as zoning for conservation.

C. **Shoreline regulation** - zoning laws that reflect environmental as well as health and safety concerns; usually require zoning of all lands within a given distance of all navigable waters in each state; generally include tree-cutting rules, setback requirements for structures, filling and grading controls, dredging regulations, minimum standards for water supply and waste disposal, minimum lot sizes and widths, and subdivision regulations.

D. **The Federal Emergency Management Association (FEMA)** requires the purchase of Flood insurance for homes built within their designated flood zone.

IV. Health and Safety Codes

A. **Building codes**

1. Specify construction standards that must be met when erecting, maintaining, or demolishing buildings.
2. Generally identify requirements for electrical wiring, sanitary equipment, and fire-prevention standards.
3. Enforced by issuing building permits that verify compliance with building codes and zoning ordinances.
4. The building inspector issues a certificate of occupancy when the completed structure has been inspected and found satisfactory.

5. Issuing a building permit does not take precedence over the violation of a deed restriction.

V. Environmental Concerns

A. **Pollution and environmental risks in real estate transactions**

1. Increasing public awareness of and concern about pollution problems and their health and economic effects have had significant consequences on real estate sales and values.
2. The actual dollar value of real property can be affected significantly by both real and perceived pollution.
3. The cost of cleaning up and removing pollution may be much greater than the dollar value of the property before pollution occurred.
4. In some areas of the United States, mortgage and title insurance approval may depend on the inspection of the property for hazardous substances and proof of their absence.

B. **Role of real estate licensees** regarding environmental risks in real estate transactions

1. Be alert to the possibility of pollution and hazardous substances on the property being sold.
2. Ask clients about the possibility of hazardous substances associated with the property.
3. Expect increasing numbers of questions from customers concerned about pollution.
4. Consider the consequences of the potential liability in real estate transactions where hazardous substances may be involved.
5. Contact government agencies and private consulting firms for information, guidance, and detailed study; real estate licensees often, however, do not have the technical expertise required to determine whether hazardous material is present on or near the property.
6. Be scrupulous in considering environmental issues and exercise a high degree of care in all real estate transactions.

C. **Hazardous substances of concern to real estate professionals**

1. **Radon gas** - an odorless radioactive gas produced by the decay of radioactive materials in rocks under the earth's surface.
    a. Radon is released from the rocks and finds its way to the surface; usually it is released into the atmosphere. Radon comes into a house through holes in the foundation or basement or crawl space.
    b. Long-term exposure is believed to cause lung cancer.
    c. The U.S. Environmental Protection Agency (EPA) has established radon levels that are thought to be unsafe.
    d. Testing techniques have been developed that allow homeowners to determine the exact quantity of radon in their homes.
    e. If a home is determined to have radon gas, the seller may, if the contract requires, be obligated to remediate the hazard, whether the danger is actual or only perceived.
    f. Most homes with elevated levels of radon can be fixed for between \$500 and \$2,500, with an average cost of about \$1,200.
2. Asbestos - material used for many years as insulation on plumbing pipes and heat ducts and as general insulation because it is a poor heat conductor; also was used in floor tile and roofing material.
    a. Relatively harmless if not disturbed; can become life-threatening during its removal because of accompanying dust.
    b. Exposure to asbestos dust may exist if
        (1) the asbestos ages and starts to disintegrate. This disintegration is referred to as being friable.
        (2) remodeling projects include the removal of asbestos shingles, roof tile, or insulation that can cause the dust to form in the air and expose people in the area to the

health hazard.

3. **Urea-formaldehyde foam insulation (UFFI)** - a synthetic material generally used to insulate buildings prior to 1978. It was banned because of its toxic out-gassing.

   The toxicity known as volatile organic compounds (VOC) escaped into a dwelling for several years after its application. Today insulators use a nontoxic spray to insulate buildings.
   a. UFFI was typically pumped between walls as a foam that later hardens and acts as an insulating material.
   b. UFFI became dangerous because of gases released from the material after installation.
4. **Lead poisoning** - lead is a mineral that has been used extensively because of its pliability, its ability to impede water flow, and its rust resistance.
   a. Becomes a health hazard when ingested.
   b. Sources of lead poisoning
      (1) Peeling or flaking paint
      (2) Water supply systems
   c. Federal regulations on lead-based paint disclosure
      (1) Owners of residential properties built before 1978, when the use of lead-based paint was banned, will have to disclose to buyers or renters the presence of known lead-based paint hazards, if known to owner (seller) or landlord.
      (2) A lead-based paint disclosure statement must be attached as a separate item to all real estate sales and lease contracts on pre-1978 residential properties.
      (3) Real estate practitioners must distribute to buyers and renters a federal lead hazard pamphlet but are not responsible for ensuring that people read and understand the brochure.
      (4) Buyers will have up to 10 days to have a lead-risk assessment performed on the property if they want one.
      (5) Exemptions from the regulations are provided for housing for the elderly and disabled, provided children are not regularly present; for vacation homes and short-term rentals; for foreclosure sales; and for single-room rentals within dwellings.
      (6) Children under six years of age are most vulnerable to exposure to lead-based paint.
5. **PCBs (polychlorinated biphenyls)** - used in the manufacture of electrical products such as voltage regulators as well as in paints and caulking materials
   a. PCBs haven't been used since 1977; however, they still are dangerous because many of the products containing them are still in operation.
   b. An environmental consultant can assess the property and recommend procedures for cleanup.
6. **Waste-disposal sites - landfill operations**
   a. Landfill - a specific site that has been excavated and should be lined with either a clay or a synthetic liner to prevent leakage of waste material into the local water system.
   b. Construction and maintenance of a landfill operation is heavily regulated by state and federal authorities.
   c. Landfills at improper locations and improperly managed sites have been sources of major problems; for example, landfills

constructed in the wrong type of soil will leak waste into nearby wells, causing major damage.
   d. Real estate licensees must be aware of such facilities within their areas and take appropriate steps when dealing with potential clients.

7. **Underground storage tanks** - used in residential and commercial settings for many years.
   a. In the United States there are an estimated 3 million to 5 million underground storage tanks that hold hazardous substances such as gasoline.
   b. Risk occurs when containers become old, rust, and start to leak.
   c. Toxic material may enter the groundwater, contaminate wells, and pollute the soil.
   d. Sources of pollution
      (1) Older gas stations with steel tanks that develop leaks through oxidation (rusting).
      (2) Underground containers used to hold fuel oil for older homes
   e. Recent federal legislation calls for removal of such tanks and all the polluted soil around them.
8. **Groundwater contamination**
   a. Groundwater includes runoff at ground level as well as underground water systems that are sources of wells for both private and public facilities.
   b. Sources of contamination
      (1) Waste-disposal sites
      (2) Underground storage tanks
      (3) Pesticides and herbicides typically used in farming communities
   c. The only protection for the general public against water contamination is heavy government regulation.
   d. Once contamination is identified, its source can be eliminated; the process often is time-consuming and may be very expensive.
9. **Electromagnetic fields (EMFs)** - generated by movement of electrical currents.
   a. High-tension power lines reflect a major concern with regard to EMFs.
   b. The potential for EMFs being a health hazard is a source of controversy; however, they are suspected of causing cancer and related health problems.
   c. Real estate licensees should be aware of continuing research on EMFs.
10. **Mold** - an organism that may cause allergic reactions and, therefore, is an environmental issue. Annual maintenance checks (around toilets, showers, and sinks) help to detect mold in its early stages. Dehumidifiers, proper ventilation, perimeter drainage, and sump pumps help avoid mold by removing water from the property. Most homeowners' insurance companies set dollar limits for mold claims or make mold problems an exclusion to the homeowner's policy.
   a. Common varieties of mold can cause allergic reactions as well as asthma episodes, infections, and other respiratory problems, but they do not emit toxins.
   b. Very little is known about toxic molds like *Stachybotrys chartarum*, often referred to as "black mold." In sufficient amounts this mold can be dangerous and has been associated with severe health problems and substantial contamination of buildings.
   c. Disclosure of mold contamination is not currently required by the federal government.

d. The EPA has established guidelines to deal with mold problems for schools and commercial buildings.

D. **Agencies administering federal environmental laws**

1. **Environmental Protection Agency (EPA)**
    a. **Toxic Substance Control Act**
    b. **Resources Conservation and Recovery Act**
    c. **Federal Clean Water Act**
2. **U.S. Department of Transportation** - administers the Hazardous Materials Transportation Act
3. **The Occupational Safety and Health Administration (OSHA)** and the U.S. Department of Labor - administer standards for all employees working in the manufacturing sector
4. Federal government encourages state and local governments to prepare legislation in their areas

E. Statutory law

1. **Resource Conservation and Recovery Act (RCRA)** of 1976 - created to regulate the generation, transportation, storage, use, treatment, disposal, and cleanup of hazardous waste.
2. **The Comprehensive Environmental Response Compensation & Liability Act (CERCLA)** was created in 1980.
    a. **Established fund of $9 billion called Superfund** to clean up uncontrolled hazardous waste dumps and respond to spills.
    b. Created a process for identifying liable parties and ordering them to take responsibility for cleanup.
    c. Liability under Superfund consideration to be strict, joint and several, and retroactive.
        (1) **Strict liability** - owner is responsible to the injured party without excuse.
        (2) **Joint and several liability** - each individual owner personally responsible for the damages in whole; if only one owner is financially able to handle the total damage, that owner will have to pay all of it and attempt to collect the proportionate share of the rest from the owners.
3. **Leaking Underground Storage Tanks (LUST) regulations -** established in 1984
    a. Governs the installation, maintenance, monitoring, and failure of underground storage tanks
    b. Aimed at protecting groundwater in the United States through release prevention, detection, and correction
4. **Superfund Amendments and Reauthorization Act (SARA) -** created in 1986
    a. Established stronger cleanup standards for contaminated sites
    b. Substantially increased the funding of the Superfund
    c. Attempted to clarify the obligation of the lenders
    d. Created the concept called innocent landowner immunity

F. **Agents' Responsibilities**

1. Most state laws DO NOT hold listing agents or buyers' agents to a standard of discovery. This is why most states have passed a seller's property disclosure act. With this new legislation the burden to disclose both known and latent property defects (to the buyer) is shifted to the seller. However, if listing agents know or have been made aware of the material defect, they must obviously disclose what they know. A buyer's agent is held to the same standard. Discovery, no. Disclosure, yes.

VI. Deed Restrictions or Covenants

A. **Private restrictions written into deeds or leases that limit the use of property -** for example, restrictions on the type or size of the building.

B. May be terminated by the affected necessary parties by a quitclaim deed or mutual release properly recorded.

C. **Generally enforced by means of a court injunction.**

D. **Adjoining lot owners** in a subdivision can lose the right to the court's injunction by inaction, under the doctrine of laches (the loss of a right through undue delay or failure to assert the right).

E. **Deed restrictions** or covenants differ from deed conditions in that violation of a condition can give the grantor the right to take back ownership; this right does not apply where a violation of a private restriction occurs.

VII. Water Rights

A. **Riparian rights -** rights of owners of land adjacent to a river or stream

B. **Littoral rights -** rights of owners adjacent to commercially navigable lakes, seas, and oceans.

C. **Amount of land owned adjacent to water may be affected by the following:**

1. **Accretion** - land increase caused by water's action leaving soil deposits; if water recedes, new land would be acquired by reliction.
2. **Erosion** - the slow loss of soil caused by wearing away of land by wind or rain.
3. **Avulsion** - sudden loss of land caused by act of nature such as an earthquake.
4. **Doctrine of prior appropriation -** with exception of limited domestic use, right to use water is controlled by the state instead of the owner of land adjacent to the water.
5. **Alluvion -** an increase in land ownership created by the gradual addition of deposited matter from running water. Alluvion is the clay, silt, sand, or gravel deposited by accretion.

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NATIONAL TEST TOPIC #8

LAND USE & GOVERNMENT CONTROLS #8

2020 Practice Classroom Quiz

1. A landowner constructed a building seven stories high. Several years later, the municipality changed the zoning ordinance, prohibiting buildings that exceed six stories in height. Which of the following is *TRUE* regarding the existing seven-story building?
A) It is a nonconforming use.
B) The building must be demolished.
C) It is a conditional use.
D) The owner must obtain a variance.

2. Control by zoning ordinances does *NOT* regulate the
A) height of buildings in an area.
B) density of population.
C) use of the property.
D) price of the property.

3. The federal Interstate Land Sales Full Disclosure Act provides that
A) sales of lots in subdivisions consisting of more than 25 lots are exempt from regulation.
B) developers file with HUD before selling certain properties interstate.
C) sales of lots in subdivisions of ten acres or more are exempt from regulation.
D) potential purchasers be issued a written report with detailed information about the subdivision before closing.

4. Which statement is *TRUE* about land taken for public use?
A) The owner must be fairly compensated.
B) The health, safety, and welfare of the government must be the reason.
C) The local use will benefit the residents in the immediate area.
D) The property is then established as a fee simple determinable estate for a particular use.

5. If a buyer builds an outbuilding that violates the subdivision covenants mentioned in his deed, he
A) may forfeit the title to the property.
B) may be sued and required to alter the structure or remove it.
C) may be sued and required to pay damages to the other residents in the neighborhood.
D) is safe from legal actions taken by other residents in the area about this matter.

6. A town prohibits a developer from building more than five houses per acre in a subdivision. This restriction is called
A) a variance.
B) density zoning.
C) cluster building.
D) curvilinear development.

7. For the past 30 years, a business owner has operated a neighborhood grocery store. Last week the city council passed a zoning ordinance that prohibits packaged food sales in the area where her grocery store is located. The store is now an example of a(n)

A) illegal enterprise.
B) nonconforming use.
C) violation of the zoning laws.
D) variance of the zoning laws.

8. Restrictive covenants

A) are no longer effective when the title is transferred.
B) apply only until the developer has conveyed the title.
C) can be removed by a court of competent jurisdiction.
D) apply to and bind successive owners of the property.

9. The construction of a family room, additional bedroom, and extra bath has been completed on the owner's home. Before the addition can be used, which of the following is *TRUE?*

A) The municipality must issue a building permit.
B) The bath must be inspected by the plumbing inspector.
C) The municipality must issue an occupancy permit.
D) The municipality must issue a conditional-use permit.

10. A wooded area with biking and hiking trails is situated between old cotton mills and a housing development. This area is considered a

A) designated park required under federal guidelines.
B) variance to the existing zoning.
C) utility easement.
D) buffer zone.

11. A man applies to the municipality for permission to open an adult day-care facility in his neighborhood. He may be granted a(n)

A) variance.
B) nonconforming use permit.
C) amendment to the zoning ordinance.
D) conditional-use permit.

12. Under an existing ordinance no signs that extend more than three feet above the highest point of a roof may be placed on any building. An owner wants to erect a nine-foot-high revolving sign on the roof of his store. In order to do this legally, the owner must get a

A) deed to the air rights.
B) variance.
C) nonconforming use permit.
D) court order.

13. All of the following are examples of public land-use control *EXCEPT*

A) zoning ordinances.
B) building codes.
C) restrictive covenants.
D) city planning requirements.

14. A man owns property next to property that the city has condemned to extend the runways at the municipal airport. The man feels his property has diminished in value due to this public use. He may seek compensation by an action of
A) taking.
B) condemnation.
C) confiscation.
D) inverse condemnation.

15. Deed restrictions may *NOT* legally control or limit
A) sizes and types of structures to be built.
B) potential future uses of the properties.
C) the race of future owners and occupants of a property.
D) exterior finish and decoration of the structures.

16. The condemnation of private property for public use is allowed under the state's right of
A) police power.
B) escheat.
C) eminent domain.
D) confiscation.

17. A subdivision was developed, and one of the deed restrictions covering all of the properties in the subdivision set aside the back six feet of each parcel as a combination green belt area and bicycle path. A homeowner plans to convert the back one-half of her yard, including this set-aside space, into an organic garden. Her neighbor can
A) do nothing because individual homeowners have no authority in this matter.
B) go to court in an attempt to obtain an injunctive relief.
C) force the homeowner to sell her property.
D) share in the bounty from the organic garden.

18. The purpose of bulk zoning is to
A) ensure that certain kinds of uses are incorporated into developments.
B) specify certain types of architecture for new buildings.
C) control density and avoid overcrowding.
D) set overall development goals for the community.

19. The plat for a proposed subdivision is submitted to the
A) municipality.
B) property owners.
C) developer.
D) state.

20. Deed restrictions are created by all of the following *EXCEPT*
A) deed.
B) statute.
C) written agreement.
D) general plan of a subdivision.

21. Zoning ordinances normally define specific uses for land that are permitted within a municipality. All of the following are designated uses in such ordinances *EXCEPT*
A) industrial.
B) commercial.
C) residential.
D) rental.

22. A municipality establishes development goals in its
A) subdivision regulations.
B) restrictive covenants.
C) environmental regulations.
D) comprehensive plan.

23. Which of the following is a variance?
A) Exception to a zoning ordinance
B) Court order prohibiting certain activities
C) Reversion of ownership
D) Nullification of an easement

24. The purpose of building permits is to
A) generate revenue for the municipality.
B) control the activities of building inspectors.
C) ensure compliance with building codes.
D) prevent encroachments.

Answer Key - **TOPIC:8: LAND USE & GOVERNMENT CONTROLS**

1. A
2. D
3. B
4. A
5. B
6. B
7. B
8. D
9. C
10. D
11. D
12. B
13. C
14. D
15. C
16. C
17. B
18. C
19. A
20. B
21. D
22. D
23. A
24. C

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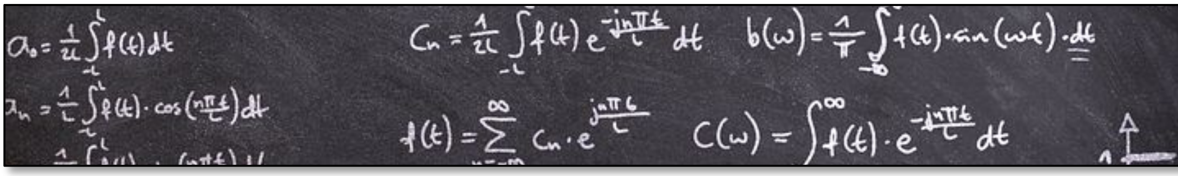
TOPIC 11

Math Questions: National Exam Portion



EXAM TOPICS

TOPIC 11 - Real estate calculations (Salesperson 10%; Broker 8%)

A. **Basic math concepts**
   1. Loan-to-value ratios
   2. Discount points
   3. Equity
   4. Down payment/amount to be financed
B. **Calculations for transactions**
   1. Property tax calculations
   2. Proration's
   3. Commission and commission splits
   4. Seller's proceeds of sale
   5. Buyer funds needed at closing
   6. Transfer fee/conveyance tax/revenue stamps
   7. PITI (Principal, Interest, Taxes and Insurance) payments
C. **Calculations for valuation, rate of return *(BROKER ONLY)***
   1. Net operating income
   2. Depreciation
   3. Capitalization rate
   4. Gross Rent and gross income multipliers

STUDY QUESTIONS and ANSWERS

I. Real Estate Calculations (Math) on National PSI Exam

1. A business tenant pays 2 percent of his total gross sales volume as rent, with a minimum base rental of $1,000 per month. In the past year, his sales totaled $435,000. How much rent did he pay?

a) $12,000

b) $ 8,700

c) $20,700

d) $ 8,460

2. Assume that the listing and selling brokers split the commission evenly. What is the sales price of a house if the listing broker received $2,593.50 and the total commission rate is 6½ percent?

a) $79,800

b) $39,900

c) $88,400

d) $76,200

3. The current taxes are $1,743.25 and have not been paid. If the sale is to be closed on August 12, what is the tax proration that will be charged to the seller based on a 360- day year?

a) $1,220

b) $660.00

c) $1,075

d) $1,104

4. A buyer offers $26,280 for a 20 percent interest in a property. What is the total value of the property?

a) $32,850

b) $131,400

c) $31,536

d) $105,120

5. An appraiser estimated the replacement cost new of a building at $560,000. The building has an estimated economic life of 40 years and an estimated remaining life of 30 years. What is the current value of the building?

a) $560,000

b) $140,000

c) $392,000

d) $420,000

6. A parcel of vacant land has an assessed valuation of $274,550. If the assessment is 85 percent of market

value, what is the market value?

a) $323,000

b) $315,732

c) $1,830,333

d) $320,000

7. If the borrower paid $189.06 interest last month on a $27,500 loan, what is the interest rate?

a) 8 ½ percent

b) 8 ¼ percent

c) 7 ½ percent

d) 7 ¾ percent

8. If a residence is valued at $87,500 and its assessment ratio is 50 percent of market value, what are the annual taxes if the tax rate of $7.80 per $100 of assessed valuation?

a) $5,608.96

b) $6,825.00

c) $3,412.50

d) $3,187.75

9. What is the cost of constructing a fence 6 feet 6 inches high around a lot measuring 90 feet by 175 feet, if the cost of erecting the fence is $1.25 per linear foot and the cost of material is $0.825 per square foot of fence?

a) $2,053

b) $1,752

c) $3,505

d) $2,083

10. A custom home containing 4,320 square feet was recently constructed on a $145,000 lot. Construction costs were $80.25 per square foot, and other fees and costs totaled $12,785. What was the total cost of the property?

a) $359,465

b) $504,465

c) $346,680

d) $145,000

11. A seller-landlord has collected the September rent from all five tenants: two pay $345 per month each

and three pay $425 per month each. Determine the prorated amount to be allowed the buyer when the sale closes on September 19.

a) $786.00

b) $1,965.00

c) $720.50

d) $1,244.50

12. A small office building sold for $949,000 and the broker received a commission of $54,990. What was the broker's commission rate?

a) 11.3 percent

b) 7 percent

c) 5.8 percent

d) 6.2 percent

13. A developer is planning a building that will contain 103,000 square feet. Construction costs are estimated to be $62 per square foot. Ninety-five percent financing is available for the structure. How much money must the developer put up to complete the project?

a) $638,600

b) $5,747.400

c) $6,066.700

d) $319,300

14. A buyer has deposited 10 percent of the sales price with the broker as earnest money, and the bank has agreed to lend $51,000, which is 80 percent of the sales price. How much additional funding must the buyer provide to complete this transaction?

a) $6,375

b) $5,100

c) $5,500

d) $6,125

15. If the annual net income from certain commercial property is $22,000 and the capitalization rate is 8 percent, what is the value of the property using the income approach?

a) $200,000

b) $183,000

c) $176,000

d) $275,000

16. The commission on the sale of a house is $4,410, and 30 percent goes to the broker who listed the

property. Of the remainder, the broker whose salesperson completed the transaction gets 45 percent, and the salesperson receives the balance. How much does the salesperson who made the sale receive?

a) $1,698

b) $1,728

c) $2,425

d) $1,389

17. A vacant lot that measures 100 feet wide by 125 feet deep is listed at a price of $250 per front foot. The broker will collect an 8 percent commission on the sale. If the lot sells for the full asking price, how much is the broker's fee?

a) $2,000

b) $1,250

c) $2,500

d) $1,500

18. A home valued at $168,500 has just had a 70 percent mortgage loan placed on it. The interest rate is 11.25 percent. The monthly payment is $1,292.22 including principal and interest. What will the principal balance of the mortgage loan be after the next monthly payment is made?

a) $117,763.56

b) $117,913.56

c) $117,950.00

d) $117,560.28

19. A property owner wishes to net $56,500 from the sale of her small building. After paying an advertising allowance of $160 and a 7 percent commission, what must the selling price be (rounded to the nearest dollar)?

a) $60,626

b) $60,925

c) $60,455

d) $60,753

20. A $75,000 mortgage loan requires a discount of $1,875 to be paid by the seller.
How many points is this equivalent to?

a) 5.0

b) 4.5

c) 2.0

d) 2.5

21. How many acres are there in the property described as it follows the NW¼ of the SW¼ of the NE¼ of Section 16?

a) 10
b) 40
c) 5
d) 20

22. Property purchased five years ago was assessed for tax purposes at 50 percent of market value. The tax rate was $4.90 per $100 of assessed valuation. Today, the taxes, imposed at the same tax and assessment rates, have increased by $637. How much has the market value of the property increased assuming straight-line appreciation?
a) $26,000.00
b) $13,000.00
c) $3,121.30
d) $6,242.60

23. The effective gross income from an office building property is $73,500, and the annual operating expenses total $52,300. If the owner expects to receive an 11 percent return on the investment, what is the value of the property?
a) $192,727
b) $475,454
c) $668,181
d) $125,800

24. A building is valued at $100,000 using a capitalization rate of 8 percent. If an investor demands a capitalization rate of 10 percent, the value of the building will:
a) Decrease more than $10.000.
b) Increase by 20 percent.
c) Increase by less than 20 percent.
d) Decrease less than $10,000.

25. A real estate licensee leased a building for ten years at an annual rent of $48,000. She will receive a commission of 7.5 percent for the first five years, 5 percent for the next three years, and 3.5 percent for the final years. What will her income be from this commission over the life of the lease?
a) $28,560
b) $30,000
c) $25,200
d) $18,000

26. Ten years ago, a family purchased a lot for $26,500. They made no improvements during the time they owned the property. Recently, they sold the lot for $62,275. What was their percentage of gross profit?
a) 235 percent

b) 42.6 percent

c) 58.2 percent

d) 135 percent

27. A lease provides that the tenant pays $760 minimum rent per month plus 4 percent of the gross sales in excess of $150,000 per year. If the tenant paid a total rent of $20,520 last year, what was the gross sales volume?

a) $285,000

b) $513,000

c) $150,000

d) $435,000

28. A 40-acre tract was sold for $2,200 per acre. The seller realized a 14.5 percent profit from the sale. What was the original cost of the tract?

a) $100,760

b) $102,924

c) $76,856

d) $75,240

29. A house was listed for sale at $84,900. The seller received $71,424 after paying the broker a 7 percent commission. What was the selling price of the property?

a) $79,345.79

b) $76,423.68

c) $76,800.00

d) $78,957.00

END

ANSWERS TO 29 MATH TYPE QUESTIONS ON NATIONAL EXAM

1. a

12 months * $1,000 per month = $12,000 minimum annual base rent; $435,000 gross sales * 2% = $8,700. Tenant paid $12,000 because minimum base rent was more than percentage of gross sales.

2. a

$2,593.50 commission split * 2 agents = $5,187 total commission; $5,187 total commission / 6.5% commission rate = $79,800 sales price.

3. c

$1,743.25 annual taxes / 360 days = $4.84 daily rate for taxes; January 1 to August 12, based on 30-day months = 222 days (7 months for January through July * 30 days +12 days in August); 222 days * $4.84 daily rate = $1,074.48 prorated taxes seller owes.

4. b

$26,280 offer / 20% interest = $131,400 total value of property.

5. d

30 years remaining life / 40 years economic life = 75%; $560,000 replacement cost * 75% = $420,000 current value.

6. a

$274,550 assessed value / 85% = $323,000 market value.

7. b

$180.06 monthly interest * 12 months = $2,268.72 annual interest; $2,268.72 annual interest / $27,500 loan amount= 8.25% interest rate

8. c

$87,500 residence value * 50% = $43,750 assessed value; $43,750 assessed value / $100 = 437.5; 437.5 *$7.80 = $3,412.50 annual taxes.

9. c

90 + 90 + 175 + 175 = 530 linear feet; 530 linear feet *$1.25 = $662.50 cost for labor; 530 feet ´ 6.5 feet = 3,445 square feet; 3,445 square feet * $0.825 = $2,842.14 cost of materials; $662.50 labor + $2,842.14 material =$3,504.64 total cost to construct fence.

10. b

4,320 square feet * $80.25 per square foot = $346,680 cost per square foot; $346,680 + $145,000 cost of lot +$12,785 other fees and costs = $504,465 total cost of property.

11. c

($345 * 2) + ($425 * 3) = $690 + $1,275 = $1,965 total rent; $1,965 / 30 days in September = $65.50 daily rent; 30 days in September - 19 days = 11 days buyer due rent; 11 days * 65.50 daily rent = $720.50 rent due to buyer.

12. c

$55,042 commission / $949,000 sales price = 5.8% (0.058) commission rate.

13. d

103,000 square feet * $62 per square foot = $6,386,000 total construction cost; 6,386,000 * 5% down payment (100% sales price – 95% amount financed) = $319,300 developer needs to complete the project.

14. a

$51,000 loan balance / 80% = $63,750 sales price; $63,750 sales price * 20% (100% sales price – 80% loan = 20% down payment) = $12,750 down payment; $63,750 sales price * 10% deposit = $6,375 earnest money; $12,750 down payment – $6.375 earnest money = $6,375 needed.

15. d

$22,000 net income / 8% cap rate = $275,000 value of property.

16. a

$4,410 total commission * 30% = $1,323 commission to listing broker; $4,410 – $1,323 listing broker commission =$3,087 remainder of commission; $3,087 * 45% =$1,389.15 commission to sales broker; $3,087 $1,389 sales broker commission = $1,697.85 commission salesman receives.

17. a

100 feet frontage * $250 per front foot = $25,000 list price; $25,000 list price ´ 8% commission rate = $2,000 broker's commission fee.

18. a

$168,500 property value * 70% = $117,950 mortgage balance; $117,950 mortgage balance * 11.25% interest =$13,269.38 annual interest / 12 months = $1,105.78 monthly interest; $117,950 mortgage balance $1,292.22 monthly P&I payment = $116,657.78 balance + $1,105.78 monthly interest = $117,763.56 mortgage balance.

19. b

$56,500 net proceeds + $160 ad allowance = $56,660; $56,660 / 93% (100% total costs – 7% commission) =$60,925 sales price.

20. d

$1,875 discount / $75,000 mortgage loan = 2.5 points.

21. a

Multiply denominators: 4 * 4 * 4 = 64; 640 acres (one section) / 64 = 10 acres.

22. a

$637 tax increase / $4.90 tax rate = 130; 130 * $100 = $13,000 assessed value / 50% (or 2 * $13,000, since100% / 50% = 2) = $26,000 increase.

23. a

$73,500 gross income – $52,300 annual operating expenses = $21,200 net income; $21,200 net income 11% return on investment = $192,727 value.

24. a

NOI of property is $8,000, which is 8% (0.08) of $100,000 value, or 10% (0.10) cap rate of $80,000; $100,000 – $80,000 = $20,000, which is a decrease of more than $10,000 to get a higher cap rate.

25. a

$48,000 annual rent * 7.5% = $3,600 annual commission ´5 years = $18,000 commission for the first 5 years; $48,000 annual rent * 5% = $2,400 annual commission * 3 years = $7,200 commission for next 3 years; $48,000 annual rent * 3.5% = $1,680 * 2 years = $3,360 commission for final years; $18,000 + $7,200 + $3,360 =$28,560 total commission over the life of the lease.

26. d

$62,275 sales price / $26,500 original sales price two years ago =235% (2.35) gross profit.

27. d

$760 per month * 12 months = $9,120 annual base rent; $20,520 total rent last year $9,120 base rent = $11,400 rent paid on gross sales; $11,400 / 4% = $285,000 sales in excess of $150,000; $285,000 excess sales + $150,000 minimum sales =$435,000 gross sales.

28. c

40 acres * $2,200 per acre = $88,000 sales price; $88,000 sales price /
114.5% (100% sales price + 14.5% profit) profit = $76,856 original cost.

29. c

$71,424 net / 93% (100% – 7% commission) = $76,800 sales price.

END

TOPIC 11 (Supplement)

Brokerage Management (Broker Only)

EXAM TOPICS

TOPIC 11 – Brokerage Management ((Broker only)

A. **Types of Ownership (Broker only)**
B. **Sales Associate Relationship (Broker only)**
C. **Agent Supervision (Broker only)**
D. **Developing Plans (Broker only)**
E. **Risk Management (Broker only)**
F. **Trust Accounts (Broker only)**
G. **Basic Financial Concepts (Broker only)**

STUDY NOTES:

I. Types of Ownership

A. **Sole proprietorship**
   1. Provides broker with flexibility and control, while trading off protection against personal liability.
   2. Appropriate for the broker who desires a small operation and sales staff.

B. **Joint or multiple ownership** - appropriate for the broker interested in growth and expansion as well as joint ownership. There are five primary forms of multiple ownership:
   1. **Corporations**
      a. **Advantages**
         (1) **Limited liability** - any liability incurred by a corporation through judgments, bankruptcies, etc., limited to the investment of a shareholder in a corporation; does not affect a shareholder's personal assets.
         (2) **Centralized management** - shareholders elect a board of

directors, who elect officers to manage the company; a licensed broker-director is responsible for the real estate brokerage phase of the business.

(3) **Continuity of life** - a corporation is a legal entity that never dies; its officers may be continually replaced if necessary.

(4) **No income limitations** - o upper limit on the amount of income a corporation may earn or the number of shareholders it may have.

(5) **Transferability** - corporate stock may be freely transferred from one shareholder to another.

b. **Disadvantages**

(1) **Double taxation** - profits taxed at both the corporate and individual levels.

(2) **Treatment of losses** - corporation losses may not be passed on to shareholders; they may be applied to future earnings of the corporation.

(3) **Capital gains** - passed on to shareholders as ordinary income.

2. **S corporations**

a. **Advantages**

(1) **No double taxation** - income, losses, and capital gains passed directly to the shareholders.

(2) **Centralized management and continuity of life** - similar to the typical corporation.

(3) **Limited liability with shareholders' interests freely transferable.**

b. **Disadvantages**

(1) **Ownership limited to 35 shareholders.**

(2) **Not more than 20 percent of income may be from passive investments,** that is, investments that are income-related, such as stock dividends or interest from deposits.

3. **General partnership**

a. **Advantages**

(1) **No double taxation** - income directly taxable to each partner.

(2) Capital gains or losses pass directly to the partners.

b. **Disadvantages**

(1) Problems arising from the death, bankruptcy, etc., of the partner(s).

(2) Personal liability.

(3) Ownership not freely transferable.

4. **Limited partnerships**

a. Rarely used in an active brokerage firm.

b. Used primarily to acquire investments such as syndicates, joint ventures.

c. One or more general partners have unlimited liability; are responsible for the operation of the business.

d. Limited partners generally have no say in the business operation.

e. Limited partners' liability is limited to the amount of the investment, unless the partners take an active role in management.

5. **Limited liability companies**

a. Offer advantages of the single-level taxation of a partnership and the limited liability of a corporation.

b. Avoid some of the restrictions that are imposed on an S corporation.

c. Must generally have at least one member; members may be corporations, individuals, limited or general partnerships, a trust, or foreign persons.

d. May be directly managed by members, or responsibility may be delegated to a property manager.

C. **Franchises and alternatives** - the broker may choose among various types of operations.

1. **Remain independent** - provides pride of ownership.
2. **Become a member of a referral system.**
3. **Franchise membership** - for example, Century 21 and Electronic Realty Associates (ERA).
    a. **Advantages**
        (1) **Approaches to management and marketing** - members pay an initial fee and a percentage of the profits in return for franchise "expertise."
        (2) **Client referral system.**
        (3) **Economics** of volume purchasing of equipment, signs, etc.
        (4) **National advertising and promotion.**
    b. **Disadvantages**
        (1) **Loss of individual identity.**
        (2) **High initial fees and franchise fees.**
        (3) **Possibly limited geographic area.**
4. **Quasi-franchise membership** - for example, GMAC and Gallery of Homes.
    a. The broker may retain the name as part of the firm identification.
    b. Offer varied services that are less extensive than those of a franchise operation - for example, Help-U-Sell.
    c. The owner is guided by a broker on how to sell property.
    d. The seller takes on part of the broker's responsibility such as showing the property.
    e. The seller generally pays a commission less than that charged by a traditional broker.
    f. **Advantages**
        (1) The broker's monetary investment and time are less.
        (2) Greater exposure to FSBOs (For Sale by Owner).
    g. **Disadvantages**
        (1) Lower fees require increased business activity.
        (2) Increased pressure to earn a profit.
        (3) May retain offices while pooling advertising outlays and sharing in the profits of the cooperative.
5. **Membership in broker association** - single office composed of a group of individual brokers who share office space and expenses.
6. **100-percent commission office**
    a. Landlord-broker owns the office and facilities; rents the office to other brokers or associates on a per-desk basis.
    b. Each broker or associate pays a monthly fee to cover the landlord's office expenses and a small percentage of the commission for the benefit of all the brokers and associates; the 100-percent concept often is used in combination with other forms of operation.

D. **Internal structure of organization**
1. **One-person organization**
2. **One-agent to ten-agent organization**
    a. A small, centralized operation in which the capacity for doing business grows as the size of the organization grows.
    b. Management responsibility, as well as the need for office space and equipment, will increase the cost of doing business.
3. **Monolithic organization**
    a. Functions as single unit, though it normally consists of a number of work groups.
    b. There is a single source of authority at the top of the organization.
4. **Decentralized organization** - fewer levels of management, thus the managers have the authority to operate essentially as individual business units.

II. Sales Associate Relationship

A. **Independent contractor**
1. The salesperson is under the supervision of the broker.

2. The salesperson contracts with the broker to produce specific outcomes - for example, leasing commissions and real estate sales.
3. The process by which a salesperson produces a commission cannot be controlled by the broker except within the guidelines of the contract.
4. The broker may not unduly restrict the methods that the associate may use.
5. The broker may not withhold federal and state income taxes, Social Security taxes, or state unemployment insurance from commissions.
6. The broker may not provide health insurance or pension plans.
7. The salesperson must pay his or her own license fees and board dues.
8. The salesperson is responsible for car and transportation expenses.
9. The salesperson may not be required to attend sales meetings.
10. The salesperson may not be required to follow a set work schedule.

B. **Employee**
1. The broker can employ, guide the activities of, maintain the standards of conduct of, or terminate an employee at will.
2. The broker is required to withhold federal and state income taxes, pay an employee's share of Social Security taxes, and withhold state unemployment insurance from commissions.
3. The broker may choose to provide fringe benefits such as health insurance.
4. The broker may require attendance at sales meetings.

C. **Federal income tax requirements to be classified as an independent contractor** - see "**VII. IRS regulations**," https://www.irs.gov/businesses/small-businesses-self-employed/independent-contractor-defined

III. Agent Supervision (broker only)

A. **A broker is responsible for supervising the activities of any salesperson employed by the broker.**

B. **Supervision includes but is not limited to the following:**
1. Reviewing all documents related to transactions.
2. Providing all licensed employees with written statement of procedures under which the office and employees shall operate with respect to handling documents related to transactions.
3. Assuming responsibility for preparation, custody, safety, and correctness of all entities on real estate forms, closing statements, and other records, even though another entity may have those responsibilities.

C. **Antitrust guidelines include but are not limited to the following:**
1. Broker should provide ongoing education on antitrust.
2. Salespeople must promote company and base fees of services provided rather than comparison with competitive forms.
3. Salespeople must avoid communication with competing forms that might be interpreted as boycotts or price fixing.
4. Policy and procedures manual must include policies for antitrust compliance.

D. **Fair housing guidelines include but are not limited to the following:**
1. Broker should provide ongoing education on fair housing.
2. Broker should be sure that salespeople do not provide assistance reluctantly to members of protected classes.
3. Salespeople should not differentiate in the quality of service offered to members of protected classes.
1. Salespeople should not falsely represent that a property is sold or refuse to write an offer for members of protected classes.
2. Salespeople should not suggest that members of protected classes would not be comfortable in a neighborhood.

E. **Americans with Disabilities Act guidelines include but are not limited to the following:**
1. Salespeople should avoid referring to a person's disability.
2. Avoid using the word *special* in dealing with someone who is disabled.
3. Avoid patronizing people with disabilities.
4. Brokers should make sure office is accessible to those with disabilities.

5. Be able to communicate with people with hearing deficits.

IV. Developing Plans

A. **Purpose** - to commit broker's financial and human resources to those activities that will produce the highest return on investment.

1. Plans tell what broker's company wants to accomplish and provide general framework for how organization will follow through.
2. The broker must have specific goals for the company to accomplish.

B**. Business plan** - generally a three-year to five-year blueprint for the organization.

C. **Short-range plan** - tells company what it should be doing in the coming year.

D. **Mission statement** - states what a company's purpose is for doing business, specifically, what the business does and where the company intends to be in the future.

V. Risk Management

A. **Management styles**

1. **Dictatorial style** - the manager has total control over the organization.
2. **Autocratic style -** managers are authoritarian but more benevolent than dictatorial managers.
3. **Participative style** - more democratic than above styles; utilizes talents of people to a greater extent than is common in other styles of management.
4. **Laissez-faire** - manager doesn't exercise any authority; style characterized by nonintervention and indifference.

B. Benefits of training program

1. **Reputation** - reputation for good program attracts new salespeople.
2. **Supervision** - need for close supervision reduced.
3. **Selection** - helps the broker select the most promising salespeople.
4. **Motivation** - motivates salespeople to try out what they have learned.
5. **Morale** - aids the retention of salespeople by helping them to be productive as quickly as possible.
6. **Less turnover** - provides the knowledge that is necessary for salespeople to succeed, thus reducing the need to terminate the unproductive.

C. **Objectives of a training program**

1. **Good habits** - primary objective to develop good working habits in trainees.
2. **Increased profits** - provides well-chosen salespeople with greater profits.
3. **Better production** - providing salespeople with training as well as attention increases their productivity.
4. **Better time management** - lessens the need for salespeople to depend on brokers, thus allowing greater sales production.
5. **Learning from mistakes** - makes salespeople aware of the need to learn from mistakes.

D. **Personal assistants**

1. Personal assistants may handle the non–sales-related aspects of real estate transactions.
2. Personal assistants have enhanced the productivity of salespeople as well as the profitability of brokerage firms.
3. State licensing laws may address the numerous issues posed by the use of personal assistants.
4. Personal assistants generally are hired and supervised by a salesperson.
5. The broker's policies and procedures should define how salespersons' assistants are handled in an organization.

E. **Recordkeeping**

1. Method of keeping financial records
   a. Cash method - records income as received and expenses when actually paid.
   b. Accrual method - records income when earned and expenses when incurred (most firms begin operating under the cash method because the accrual method is more complicated.)
2. **Financial analysis guidelines**
   a. Provides standardized method of classifying income and expenses;

accounting functions are becoming computerized.

b. After expense categories have been established and income categories assigned, the coding of deposit slips and checks written can provide the basis for the development of financial statements, balance sheets, and profit-and-loss statements.

3. **Typical bookkeeping system**
    a. **Records of income -** can be entered on a general ledger page as in a checkbook register or on a computer and on individual ledgers to reconcile the trust account.
    b. **Record of payments -** carbon copy of entries, duplicate of check, or computer record is sufficient.
    c. **Accounts payable -** list all the bills received and the date of payment in the file or book.
    d. **Payroll card -** shows the gross and net salaries plus the federal and state tax deductions for all employees.
    e. **Commission records -** indicate the amounts of all commissions paid to each salesperson, with each transaction identified.
    f. **Advertising -** newspaper, Internet, cable TV, etc., ads are checked for accuracy and charted to keep track of calls received.
    g. **Telephone -** outgoing personal calls should be discouraged as much as possible by logging incoming and outgoing calls or by computer printouts.
    h. **Supplies -** a sign-in/sign-out sheet should be used to keep track of such items as lawn signs and lock boxes.
4. **Miscellaneous**
    a. **Licensing requirements -** brokers should make sure that salespeople are licensed properly.
    b. **Contracts -** each person in the office should sign the contract; this is essential for the independent contractor.
    c. **Policy manual -** the office policy and procedure manual should be ready when a brokerage office is opened.
    d. **Legal advice -** brokers should retain good attorneys for sound legal advice.

VI. Trust Accounts

A. Commingling business monies with escrow monies is illegal.

B. Trust account records must be kept of the names of parties for whose benefit the trust account is created; most brokers maintain trust account records on computer.

C. Notation of the date of receipt of any sum and the record of the date and manner of disbursement of funds held in trust should be maintained.

D. All disbursement notations should include the check number and the name of the payee.

E. Trust funds should be deposited in a checking account maintained especially for this purpose.

VII. Basic Financial Concepts

A. **Cash flow -** net spendable income from the investment calculated by deducting all the operating and fixed expenses from the gross income.

B. **Company dollar -** amount of income that remains after subtracting all the commissions from the gross income.

C. **Gross income -** revenue earned from all sources, including sales, appraisals, management fees, etc.

D. **Budget -** a quantified business plan.

E. **Budgeting process -** mechanism through which a broker can design a firm's activities and assign dollar costs and anticipated revenues to their implementation.

F. **Zero-base budgeting -** requires thatall budgeted costs for the planning period be justified each time a new budget is developed.

G. **Desk cost -** the cost of providing the opportunity for salespeople to conduct business is calculated by dividing the total operating expenses of the firm (including salaries, rent, insurance, etc.) by the number of salespeople. (The number of desks is not considered in the calculation. For example, if the broker's annual overhead is $60,000 and there are two desks, each accommodating two salespeople, the desk cost for the firm is $15,000. On a 50/50 split, each salesperson does not begin to earn a profit for the broker until each has brought in a total of $30,000 in gross commissions for the year.)

END