REAL ESTATE FINANCE

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Preface

Real estate is bought with borrowed money, and the machinery that supplies, prices, secures, and recovers that money is the subject of this book. Real estate finance is where law, mathematics, and institutions meet. A student who understands it can explain why a loan costs what it costs, who ultimately funds it, what document gives the lender the power to foreclose, and what happens when a borrower cannot pay. A student who does not understand it can recite loan names without grasping the system that gives them meaning.

This book is written for the community college course in real estate finance that follows the introductory principles course and that prepares candidates for the finance portion of the California real estate examinations, including the broker examination, which probes finance more deeply than the salesperson examination does. The treatment is therefore quantitative as well as conceptual. The reader will calculate amortized payments, debt-to-income ratios, loan-to-value ratios, points, and yields, and will learn to read the disclosures and forms that govern a real loan.

The organizing idea is that finance is a system, not a list. Money originates in the primary market, is standardized and resold in the secondary market, is secured by instruments enforced under state law, is constrained by federal regulation and fair-lending duties, is priced and underwritten by qualifying the borrower and the property, and is recovered through default and foreclosure when repayment fails. The chapters follow that flow. The early chapters build the environment: money, interest, the Federal Reserve, the markets, and the SAFE Act. The middle chapters develop instruments, regulation, ethics, and the loan process. The next chapters survey the loan products themselves, conventional, government, alternative, and seller financing, and then turn to qualifying the borrower and the property. A mathematics chapter consolidates the calculations, and a capstone traces a single financed transaction from application to funding and through the possibility of default.

Each chapter follows a consistent pattern: learning objectives, narrative development, worked examples with the arithmetic shown step by step, key terms, review questions, a case study, and a ten-item quiz. The mathematics is not confined to one chapter; it is worked where it arises, so that a payment calculation appears alongside amortization and a ratio calculation appears alongside qualifying.

A word on scope and currency. Real estate finance is unusually sensitive to changing numbers: interest rates move daily, conforming loan limits change annually, and program terms shift with policy. This book teaches the durable structure and the methods, and treats specific figures as illustrative. Where a number appears, verify the current value before relying on it.

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About the Book

Read each chapter before the corresponding session, and work every example with a calculator and paper. Finance math rewards repetition; the licensing examination tests it under time pressure, and fluency comes only from working many problems.

Build a vocabulary of instruments and institutions. Much of finance is knowing precisely what a note, a deed of trust, a conforming loan, and a secondary-market agency each are and how they relate. Use the key terms as flashcards.

Treat the qualifying chapters as the heart of the practical course. Calculating whether a borrower qualifies, and whether a property supports a loan, is the daily work of lending, and the methods in Chapters 13 through 15 are the ones a practitioner uses most.

Use the review questions, case studies, and quizzes as diagnostics. The answer keys are in the accompanying instructor materials. The capstone in Chapter 16 assumes you have worked the math in the earlier chapters.

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CHAPTERS

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1: The Real Estate Finance Environment - Money, Interest, and the Fed

1.1 Why Finance Drives Real Estate

Real property is expensive, durable, and immovable, and almost no one buys it with cash. The typical purchase is financed: a buyer supplies a fraction of the price as a down payment and borrows the rest, repaying over many years. Because borrowing is nearly universal, the cost and availability of credit shape the entire market. When loans are cheap and easy to obtain, buyers can afford more, demand rises, and prices climb. When loans are costly or scarce, demand contracts and the market cools. The study of real estate finance is, at bottom, the study of how this credit is created, priced, secured, and recovered.

This dominance of credit has a practical consequence for the licensee. A real estate professional who cannot explain financing cannot serve clients well, because the loan is usually the part of the transaction that decides whether a deal happens at all. A buyer's real question is rarely "what does the house cost" but "what will it cost me each month, and can I qualify." Answering that question is a finance question.

1.2 Interest: The Price of Money

Interest is the price paid for the use of money over time. A lender who parts with money for years forgoes other uses of it and bears the risk of not being repaid, and interest compensates the lender for both. The amount of interest depends on three things: the principal, the amount borrowed; the rate, expressed as a percentage per period, usually per year; and the time the money is borrowed.

Interest comes in two forms, and the difference is fundamental. Simple interest is charged only on the original principal. Compound interest is charged on the principal and on previously accrued interest, so that interest itself earns interest. Most real estate loans are structured so that interest is charged on the outstanding balance each period, which behaves like simple interest within each period but, because the balance changes over the life of an amortized loan, produces the characteristic amortization pattern developed in later chapters.

Worked Example: Simple Interest

The simple interest formula applies the basic relationship of part, whole, and rate over time:

$$\text{Interest} = \text{Principal} \times \text{Rate} \times \text{Time}$$

Consider a principal of $300,000 at an annual rate of 7 percent for one year. The annual interest is:

$$300,000 \times 0.07 \times 1 = \$21,000$$

For one month, the time is one twelfth of a year, so the monthly interest is the annual figure divided by twelve:

$$\frac{\$21,000}{12} = \$1,750$$

This monthly interest charge is exactly the amount that the first month's payment on this loan must cover before any money reduces the principal. If the loan required interest only, the borrower would pay $1,750 each month and the balance would never fall. The interest calculation is the foundation of every payment calculation that follows, which is why it appears in the very first chapter.

Worked Example: Finding the Rate or the Principal

Because interest, principal, rate, and time are linked by one relationship, any one can be found from the others. Suppose a borrower paid $1,750 in interest for one month on a loan at a 7 percent annual rate, and wants to confirm the principal. Rearrange the relationship: the monthly rate is 7 percent divided by twelve, which is about 0.5833 percent, or 0.005833. The principal is the interest divided by the monthly rate:

$$\frac{1,750}{0.005833} \approx \$300,000$$

The same algebra finds a rate from a known interest and principal, or a time from the others. The licensing examination frequently gives three of the four quantities and asks for the fourth, so practicing the rearrangement until it is automatic pays off directly.

1.3 The Federal Reserve and the Cost of Money

Interest rates are not set arbitrarily by individual lenders; they emerge from a market that the Federal Reserve, the central bank of the United States, strongly influences. The Federal Reserve, commonly called the Fed, conducts monetary policy with the goals of stable prices and maximum sustainable employment, and the principal tool it uses affects the cost and availability of credit throughout the economy, including mortgage credit.

The Fed influences short-term interest rates by setting a target for the rate at which banks lend reserves to one another overnight, and by buying and selling securities in the open market, which expands or contracts the supply of money and credit. The discount rate, the rate at which the Fed itself lends to banks, is another lever. When the Fed eases policy, credit becomes more plentiful and cheaper, and mortgage rates tend to fall; when the Fed tightens, credit becomes scarcer and costlier, and mortgage rates tend to rise. The Fed does not set mortgage rates directly, and long-term mortgage rates respond to many forces, including expectations about inflation and the demand of investors for mortgage-backed securities, but the Fed's posture is among the most powerful influences on the climate in which real estate is financed.

The licensee need not master monetary economics, but should understand the direction of the effect: easier Fed policy generally supports real estate activity by lowering borrowing costs, while tighter policy generally restrains it. This explains why news about the Fed moves housing markets and why the cost of a mortgage can change substantially over the course of a year.

1.4 Inflation and Real Rates

Interest rates carry an expectation about inflation, the general rise in prices over time. A lender who will be repaid in dollars worth less than the dollars lent demands compensation for that erosion, so the stated, or nominal, interest rate includes an inflation premium. The real interest rate is the nominal rate minus expected inflation, and it reflects the true cost of borrowing in terms of purchasing power. When inflation expectations rise, nominal mortgage rates tend to rise with them. Understanding this relationship helps explain why mortgage rates can climb even when the economy seems weak: if lenders expect inflation, they price it into the loans they make.

1.5 How Rates Shape the Market

The level of interest rates affects real estate through affordability. A higher rate raises the monthly payment for a given loan amount, which reduces the amount a buyer with a fixed income can borrow, which reduces what the buyer can pay for a home. The effect is large. A change of one or two percentage points in the mortgage rate can change the affordable price for a typical buyer by a substantial margin, because the payment is so sensitive to the rate over a long amortization. This sensitivity is why finance is inseparable from market analysis: the same house is affordable to a given buyer at one rate and out of reach at a higher one. The chapters that follow develop the tools to quantify this relationship precisely.

Worked Example: Rates and Affordability in Concept

Consider a buyer who can devote $2,000 per month to principal and interest. The exact loan amount this payment supports depends on the rate and term, calculated by methods developed in the mathematics chapter, but the direction is clear and worth seeing now. At a lower interest rate, more of each $2,000 payment can go toward principal, so the buyer can support a larger loan; at a higher rate, more of each payment is consumed by interest, so the same $2,000 supports a smaller loan. If rates rise enough, the buyer who once qualified for a given home no longer does, without anything about the buyer or the home having changed. The example, though not yet fully calculated, captures the central economic fact of real estate finance: the rate is not a detail, it is often the deciding variable, and the professional who understands its effect can advise clients about timing, budgeting, and the tradeoffs among loan choices.

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2: Financial Markets, FinTech, and the SAFE Act

2.1 Two Connected Markets

Mortgage lending happens in two markets that together form a single system. The primary mortgage market is where loans are originated: a borrower applies, and a lender underwrites and funds the loan. The secondary mortgage market is where existing loans are bought and sold among investors after they are made. The connection between the two is the engine of modern mortgage finance. When a primary lender sells a loan into the secondary market, it recovers its capital and can lend again, so funds recycle continuously rather than being locked up for thirty years in a single loan.

This recycling does more than supply liquidity. Because secondary-market investors will buy only loans that meet their standards, primary lenders originate loans to those standards so the loans can be sold. The result is that lending is standardized across the country: documentation, underwriting criteria, and loan structures converge on what the secondary market will accept. The primary and secondary markets are treated in depth in their own chapters; this chapter establishes the framework and then turns to two forces reshaping the primary market, technology and the licensing of the people who originate loans.

2.2 The Rise of Financial Technology

Financial technology, commonly called FinTech, refers to the use of software, data, and automation to deliver financial services. In mortgage lending, FinTech has transformed how borrowers find loans, how applications are taken, and how underwriting decisions are made. Online application platforms let borrowers apply at any hour and upload documents electronically. Automated underwriting systems evaluate applications against secondary-market criteria in minutes rather than days, pulling credit, verifying data, and returning a recommendation. Electronic disclosures and electronic signatures move documents that once required mail and ink.

The effects are mixed and worth understanding. FinTech has made the loan process faster, more transparent in some respects, and accessible to borrowers who prefer self-service. It has also raised new concerns: the fairness of algorithms that affect credit decisions, the security of the large quantities of personal data involved, and the risk that automation obscures who is responsible when something goes wrong. The licensee operating in a FinTech-driven market should appreciate both the efficiency it brings and the duties of accuracy, privacy, and fairness that technology does not erase. The legal obligations of disclosure and fair lending, developed in later chapters, apply with full force to loans originated through software.

2.3 The SAFE Act and Loan Originator Licensing

The people who take loan applications and offer or negotiate loan terms are mortgage loan originators, and federal law requires them to be licensed or registered. The Secure and Fair Enforcement for Mortgage Licensing Act, known as the SAFE Act, was enacted in the wake of the financial crisis of the late 2000s to bring accountability and minimum standards to mortgage origination. The SAFE Act requires that mortgage loan originators be either licensed by a state or registered if employed by a federally regulated depository institution, and it established the Nationwide Multistate Licensing System, a national registry that assigns each originator a unique identifier and tracks the originator's record across states.

The Act's requirements parallel the protective logic seen throughout real estate licensing. A mortgage loan originator must generally complete prelicensing education, pass a national examination, submit to a background check including fingerprinting and a credit review, and complete continuing education to maintain the license. The unique identifier follows the originator, so a record of misconduct cannot be escaped by moving to another state. The purpose is to ensure that the individuals who guide borrowers into the largest debts of their lives meet minimum standards of competence and integrity.

2.4 Mortgage Origination Licensing in California

California presents a distinctive arrangement because two different agencies can license mortgage activity, and the licensee should understand the basic division. A real estate broker license issued by the Department of Real Estate authorizes mortgage brokerage as part of real estate activity, and an individual originating loans under that authority obtains a mortgage loan

originator endorsement that satisfies the SAFE Act through the Department of Real Estate. Alternatively, mortgage activity can be licensed under California's separate financing law administered by the Department of Financial Protection and Innovation, which licenses lenders and originators outside the real estate brokerage framework. The two pathways serve overlapping activities under different regulators, and which applies depends on the license held and the nature of the business.

The detail of these pathways is beyond a survey course, but the principle is not: anyone who originates residential mortgage loans for compensation must be properly licensed or registered and must hold a SAFE Act endorsement, and operating without the required authority is a serious violation. A real estate licensee who arranges loans must confirm that the activity is covered by the appropriate license and endorsement.

2.5 Why This Framework Matters

The market framework and the licensing regime together set the stage for everything that follows. The primary and secondary markets explain where money comes from and why loans look the way they do. FinTech explains how the modern loan process operates and why it moves quickly. The SAFE Act explains who is permitted to originate loans and the standards they must meet. A student who holds these three ideas in mind will find that the loan products, regulations, and qualifying methods in later chapters fit into a coherent structure rather than arriving as disconnected facts. Finance is a system, and this chapter sketches its outer boundaries.

Worked Example: Tracing a Loan Through the System

Follow a single loan conceptually through the framework. A borrower applies online through a lender's FinTech platform; the application is the federally standardized residential loan application that later chapters examine in detail. A licensed mortgage loan originator, holding a SAFE Act endorsement and a unique identifier in the national registry, takes the application and is responsible for its accuracy and for the required disclosures. An automated underwriting system evaluates the application against secondary-market standards, because the lender intends to sell the loan after closing. The lender funds the loan in the primary market, then sells it into the secondary market, recovering capital to lend again. The loan, now owned by a secondary-market investor, is serviced by a company that collects payments.

Notice how the chapter's elements appear together: the two markets, the technology, the licensed originator, and the standardization that comes from originating to secondary-market criteria. The example shows that no element stands alone; each is part of the system that turns a borrower's application into a funded, salable loan.

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3: The Primary Market- Sources of Loan Funds

3.1 The Primary Market Up Close

The primary mortgage market is where borrowers and lenders meet and loans are made. Understanding it means knowing who the lenders are, how they differ, and how their funding affects the loans they offer. The sources of mortgage money are varied, and each has its own appetite, cost of funds, and way of doing business. A licensee who knows the landscape can direct a borrower to a lender likely to fit, which is part of competent service.

A useful first division is between depository and nondepository lenders. Depository institutions hold customers' deposits and lend partly from that pool of funds. Nondepository lenders do not take deposits; they fund loans from other sources, often borrowing money to lend and then selling the loans to replenish their funds. The distinction affects how each is regulated and how it sources the money it lends.

3.2 Depository Lenders

Commercial banks are major originators of residential mortgages. They hold deposits, offer a wide range of financial services, and make mortgage loans both to hold and to sell into the secondary market. Their broad funding base and regulatory framework make them stable, mainstream lenders. Savings institutions, historically called savings and loan associations or thrifts, were created with a focus on residential mortgage lending and remain active in it. Like banks, they take deposits and make home loans.

Credit unions are member-owned cooperatives that take deposits from and lend to their members. Because they are not-for-profit and serve a defined membership, credit unions can sometimes offer favorable terms to members and are an important source of mortgage credit for those eligible to join.

Depository lenders share the feature that part of their lending capacity comes from the deposits they hold, which links their mortgage activity to the broader business of banking.

3.3 Nondepository Lenders

Mortgage companies, also called mortgage bankers, originate loans with their own or borrowed funds and typically sell them into the secondary market shortly after closing. A mortgage banker is a lender: it underwrites, funds, and closes loans in its own name, then usually sells them, often retaining the servicing. Because mortgage bankers exist to originate and sell, they are highly attuned to secondary-market standards and are a dominant force in residential lending.

Mortgage brokers, by contrast, do not lend their own money. A mortgage broker is an intermediary that takes a borrower's application and shops it among multiple lenders to find a suitable loan, earning a fee for arranging the loan rather than funding it. A broker can give a borrower access to many loan products from many sources, which is valuable for borrowers whose situations do not fit a single lender's box. The key distinction is that the mortgage banker funds the loan and the mortgage broker arranges it; confusing the two leads to errors about who bears risk and who is paid for what.

Other nondepository sources include insurance companies and pension funds, which are significant lenders in commercial real estate, where they seek long-term, stable returns matched to their longterm obligations. Private individuals also lend, particularly in seller financing and in smaller or unconventional deals that institutional lenders avoid.

3.4 Originating Versus Servicing

A point that confuses many students is that the lender who originates a loan is often not the party who collects payments over its life. Loan servicing is the ongoing administration of a loan after it is made: collecting monthly payments, maintaining the impound account for taxes and insurance, handling escrow disbursements, and managing default if it occurs. Servicing can be retained by the originator or sold separately, and a borrower's loan may be serviced by a company the borrower never chose, even as the loan itself is owned by a secondary-market investor.

The separation of origination, ownership, and servicing is a defining feature of modern mortgage finance and follows directly from the secondary market. When a loan is sold, the new owner may hire a servicer, and the borrower simply receives notice to send payments to a new address. The licensee should be able to explain to a borrower that a change of servicer is routine and does not change the terms of the loan, only the party administering it.

3.5 Matching Borrowers to Lenders

Because lenders differ, matching a borrower to an appropriate source is a practical skill. A borrower with a straightforward profile, good credit, steady income, and a conforming loan amount, can be well served by a bank, a credit union, or a mortgage banker offering standard products. A borrower with an unusual situation, self-employment income, a non-conforming loan size, or a property type that some lenders avoid, may be better served by a mortgage broker who can shop among many sources to find one that accepts the situation. A member of a credit union may find favorable terms there. A commercial borrower may look to insurance companies or specialized lenders. The licensee does not make the loan, but knowing which kind of lender tends to fit which kind of borrower allows the professional to point clients in a productive direction and to set realistic expectations.

Worked Example: Choosing a Source

A self-employed borrower with strong but variable income, an excellent credit history, and a need for a loan slightly above the conforming limit asks an agent where to seek financing.

Reason through the Landscape

The loan amount above the conforming limit makes this a jumbo loan, which not every lender offers and which falls outside the standard secondary-market channel. The self-employment income complicates documentation, because income must be established from tax returns and business records rather than simple pay stubs. A mortgage broker is often a sensible starting point here, because the broker can shop the application among multiple lenders, including those that specialize in jumbo loans and in self-employed borrowers, rather than betting the borrower's chances on a single institution's appetite. A large bank with a portfolio jumbo program might also fit, since banks sometimes hold jumbo loans rather than selling them. The example shows the payoff of knowing the sources: the right match depends on the loan size, the income type, and which lenders are comfortable with both.

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4: The Secondary Market and the Federal Credit Agencies

4.1 Why a Secondary Market Exists

A primary lender that made a thirty-year loan and held it would have its capital tied up for thirty years, able to make only as many loans as its own funds allowed. The secondary mortgage market solves this problem by buying loans from primary lenders, returning their capital so they can lend again. The secondary market thus supplies liquidity, the continuous recycling of funds that lets the mortgage system make far more loans than primary lenders could fund on their own. It also spreads risk, moving loans from local originators to a broad base of investors, and it standardizes lending, because investors buy only loans that meet their criteria.

The existence of a deep secondary market is one reason mortgage credit in the United States is abundant and relatively uniform. A borrower in one state can obtain a loan on terms much like a borrower in another, because both loans are made to standards that the same national investors will buy. This chapter examines the institutions at the center of that market and the standards they set.

4.2 Fannie Mae, Freddie Mac, and Ginnie Mae

Three institutions dominate the secondary market, and their names and roles are staples of the licensing examination.

The Federal National Mortgage Association, known as Fannie Mae, buys conforming conventional loans from primary lenders, pools them, and issues securities backed by the pooled loans to investors. By standing ready to buy, Fannie Mae gives primary lenders confidence that the loans they originate can be sold, which keeps funds flowing into the primary market.

The Federal Home Loan Mortgage Corporation, known as Freddie Mac, performs a parallel function, also buying conforming conventional loans, pooling them, and issuing securities. Fannie Mae and Freddie Mac together set the conforming standards that define mainstream conventional lending, and their combined activity makes the conventional conforming loan the default product of American mortgage finance.

The Government National Mortgage Association, known as Ginnie Mae, plays a different role. Ginnie Mae does not buy loans. Instead, it guarantees securities backed by government-insured and government-guaranteed loans, principally FHA and VA loans. The Ginnie Mae guarantee assures investors that they will receive timely payment on the securities, which channels investor money into the government-loan programs. The distinction matters: Fannie Mae and Freddie Mac buy conventional loans, while Ginnie Mae guarantees securities backed by government loans.

4.3 Conforming and Non-Conforming Loans

A conforming loan is one that meets the standards set by Fannie Mae and Freddie Mac, including limits on the loan amount, requirements about the borrower's creditworthiness and the ratio of the loan to the property's value, and documentation standards. Because conforming loans can be readily sold to these institutions, they are widely available and generally carry the most favorable terms.

A non-conforming loan is one that does not meet these standards. The most common reason a loan is non-conforming is size: a loan that exceeds the conforming loan limit is a jumbo loan, which cannot be sold to Fannie Mae or Freddie Mac and must be held by the lender or sold through other channels. Jumbo loans often carry somewhat different terms because they fall outside the standard secondary market. A loan can also be non-conforming because of the borrower's credit profile or other features that fall outside the conforming box. The conforming loan limit changes periodically and varies by area, with higher limits in high-cost regions such as much of California, so the current limit must always be checked rather than assumed.

The licensee should grasp the practical consequence: whether a loan conforms determines which channel finances it and often affects its rate and terms. A borrower near the conforming limit may benefit from structuring the loan to stay within it, a planning point a knowledgeable professional can raise.

4.4 Mortgage-Backed Securities

The mechanism by which the secondary market funds lending is the mortgage-backed security. When Fannie Mae, Freddie Mac, or an issuer guaranteed by Ginnie Mae pools many individual loans, it issues securities representing claims on the cash flows from that pool, the borrowers' monthly payments of principal and interest. Investors buy these securities, and their money flows back through the system to fund new loans. The borrowers' payments pass through to the investors, less fees for guaranteeing and servicing.

Mortgage-backed securities transformed mortgage finance by connecting individual home loans to the vast global capital markets. An investor anywhere can, in effect, fund a portion of thousands of American mortgages by buying a security, and the homeowner's monthly payment becomes the return on that investment. This connection is why mortgage rates respond to conditions in the broader bond market and to investors' demand for these securities, not only to the Federal Reserve. Understanding the security explains why the secondary market is so powerful: it turns illiquid, long-term loans into tradable instruments that draw on a deep pool of capital.

4.5 How Secondary Standards Shape Primary Loans

The most important practical lesson of this chapter is that the secondary market's standards reach back into the primary market and shape the loans borrowers actually receive. Because a primary lender intends to sell most loans, it originates them to be salable, which means following the conforming criteria for documentation, ratios, credit, and appraisal. The automated underwriting systems that evaluate applications encode these criteria. When the secondary market tightens its standards, primary lenders tighten in turn, and borrowers find loans harder to obtain; when standards loosen, credit becomes more available. The borrower across the desk from a loan officer is, in a real sense, being evaluated against the standards of distant investors who will ultimately own the loan. This is why the qualifying methods studied in later chapters track secondary-market criteria so closely.

Worked Example: Conforming Versus Jumbo

A borrower in a high-cost California county is buying a home and needs to borrow an amount near the area's conforming loan limit. The borrower is weighing whether to make a slightly larger down payment to bring the loan just under the limit, or to borrow slightly more and accept a jumbo loan.

Reason through the Tradeoff

If the loan stays at or under the conforming limit, it can be sold to Fannie Mae or Freddie Mac, which generally means readier availability and often a more favorable rate, because the loan flows through the standard secondary channel. If the loan exceeds the limit, it becomes a jumbo loan, which the lender must hold or sell through other channels, often on somewhat different terms. By increasing the down payment enough to bring the loan under the conforming limit, the borrower may secure better terms, at the cost of more cash at closing. The example shows why knowing the conforming limit and its effect is not academic: it can change the structure of a borrower's loan and the rate the borrower pays, and a professional who raises the point adds real value.

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5: Finance Instruments- Notes, Mortgages, and Trust Deeds

5.1 Two Instruments, One Loan

A secured real estate loan rests on two documents working together. The promissory note is the borrower's written promise to repay the debt; it creates the personal obligation and states the amount, the interest rate, the payment terms, and the maturity. The security instrument pledges the real property as collateral for that debt, giving the lender the right to force a sale of the property if the borrower fails to pay. The note is the debt; the security instrument secures it. This pairing, introduced in the principles course, is the legal core of finance and deserves close attention here because the broker examination probes it in detail.

The relationship has practical consequences. The note can exist without security, in which case the lender has only the borrower's personal promise and must sue on the debt to collect. The security instrument has no independent life; it secures a specific note, and when the note is paid the security must be released. When a loan is sold in the secondary market, the note is negotiated to the buyer and the security follows it, because a security instrument separated from its note secures nothing.

5.2 Hypothecation

A defining feature of real estate finance is hypothecation: the borrower pledges property as security for a debt while retaining possession and use of it. The borrower lives in the home, or operates the building, throughout the loan, even though the property stands as collateral. This distinguishes a real estate loan from a pawn, where the lender takes possession of the collateral. Hypothecation is what allows a family to occupy the very home that secures the loan that bought it. The lender's interest is a security interest enforceable on default, not a present right to possess; the borrower's possession continues unless and until foreclosure.

5.3 The Mortgage

The mortgage is a security instrument involving two parties. The borrower, the mortgagor, gives the mortgage to the lender, the mortgagee, pledging the property as security. If the borrower defaults, the mortgagee enforces the security through judicial foreclosure, a court-supervised process. The mortgage is the historic security instrument and remains common in many states, but in California it is far less used than the deed of trust, for reasons that turn on the foreclosure method.

5.4 The Deed of Trust

The deed of trust is a three-party security instrument and the dominant one in California. The borrower, the trustor, conveys title to a neutral third party, the trustee, to hold for the benefit of the lender, the beneficiary, as security for the loan. The trustee holds what is often described as bare or naked legal title, for the limited purpose of security, while the trustor retains possession and use under the principle of hypothecation. The crucial feature is the power of sale: the trustor grants the trustee the authority to sell the property without a lawsuit if the trustor defaults, enabling nonjudicial foreclosure. When the loan is paid in full, the beneficiary directs the trustee to reconvey the property to the trustor by a deed of reconveyance, releasing the security.

The three-party structure and the power of sale are the reasons the deed of trust prevails in California. Nonjudicial foreclosure under the power of sale is faster and cheaper than judicial foreclosure, which lenders prefer. The borrower, in exchange for this faster remedy, generally gains protection from a deficiency judgment in many situations, a tradeoff developed in the default chapter.

5.5 Clauses in Finance Instruments

Finance instruments contain clauses that allocate rights and risks, and the broker examination expects familiarity with the principal ones.

An acceleration clause permits the lender to declare the entire unpaid balance immediately due upon a specified default, such

as missed payments. Without it, the lender could pursue only the missed installments, making foreclosure for the full debt impractical.

A due-on-sale clause, also called an alienation clause, permits the lender to call the entire balance due if the borrower transfers the property without the lender's consent. It prevents a buyer from taking over the seller's existing loan and forces repayment or refinancing on sale, allowing the lender to reprice the loan at current rates.

A prepayment clause addresses early payoff. Some loans impose a prepayment penalty to compensate the lender for interest lost when a loan is paid off early, though consumer-protection rules sharply limit such penalties on residential loans. A loan without a penalty may be prepaid freely.

A subordination clause allows an instrument to take a lower priority than its recording date would otherwise give, which matters in development financing where a construction lender insists on first position ahead of a seller-financed land loan.

A defeasance or reconveyance provision governs the release of the security when the debt is satisfied. Under a deed of trust, the reconveyance returns title from the trustee to the trustor.

A lock-in clause, where present, restricts prepayment for a period. An assumption provision, where the loan is assumable, allows a qualified buyer to take over the loan; many modern loans are not assumable because of the due-on-sale clause.

5.6 Senior and Junior Instruments

A property can secure more than one loan, and the loans rank in priority. A first or senior instrument has first claim on the property in a forced sale; a second or junior instrument is paid only after the senior is satisfied. Priority generally follows the order of recording, first in time, first in right, subject to the exceptions and rearrangements, such as subordination, discussed in the principles course and revisited here. A purchase-money loan used to buy the home is commonly the senior loan, while a home equity loan or seller-carried second is junior.

Priority is decisive on default. If a forced sale brings less than the total owed, the senior lender is paid first and the junior lender may receive little or nothing. This is why a junior lender charges more, demands more equity, or takes other precautions: the junior position carries more risk. Understanding priority is essential to understanding the pricing and the risk of layered financing, which appears again in the chapters on alternative and seller financing.

Worked Example: Reading an Instrument's Clauses

A borrower signs a note and a deed of trust for a $450,000 home loan. The deed of trust contains an acceleration clause, a due-on-sale clause, no prepayment penalty, and the standard power of sale, and it is recorded first, ahead of a $40,000 seller-carried second deed of trust.

Decode the Consequences

The acceleration clause means that if the borrower misses payments and triggers default, the lender can demand the entire $450,000 balance, not merely the missed installments, which is what makes foreclosure for the full debt possible. The due-on-sale clause means the borrower cannot simply hand this loan to a future buyer; selling the home will let the lender call the loan due, so the buyer will need new financing. The absence of a prepayment penalty means the borrower may pay off or refinance early without a charge. The power of sale means that on default the trustee can foreclose nonjudicially, faster than a court action. Because this deed of trust was recorded first, it is the senior lien; the $40,000 second is junior and will be paid only after the first is satisfied in any forced sale, which is why the seller carrying that second took on more risk. The example shows how the clauses and priority together define exactly what the borrower agreed to and what will happen in each contingency.

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6: Federal Regulations and Required Disclosures

6.1 Why Mortgage Lending Is Heavily Regulated

A mortgage is the largest financial obligation most people ever undertake, the terms are complex, and the consequences of misunderstanding are severe. Federal law responds with a dense framework of disclosure and conduct rules designed to ensure that borrowers are informed, are treated fairly, and are protected from abusive practices. The licensee is not the party primarily responsible for compliance, which falls on the lender, but must understand the framework, because it shapes the loan process, the documents the borrower receives, and the conduct expected of everyone in the transaction. The laws in this chapter share a purpose: to correct the imbalance of information and power between a sophisticated lender and an ordinary borrower.

6.2 The Truth in Lending Act

The Truth in Lending Act, often abbreviated TILA, requires lenders to disclose the cost of credit in a standardized form so that borrowers can compare loans on equal terms. Its central concept is the annual percentage rate, the APR, which expresses the cost of the loan as a yearly rate that includes not only the note interest rate but also certain finance charges, such as some fees and points, spread over the life of the loan. Because the APR captures more than the note rate, it is usually higher than the note rate, and comparing APRs gives a borrower a truer comparison of two loans' costs than comparing note rates alone.

TILA also governs the advertising of credit. If an advertisement states certain specific terms, such as a particular down payment or payment amount, it triggers a requirement to disclose other key terms, so that an advertiser cannot lure borrowers with an attractive figure while hiding the rest. For certain loans, TILA also grants a right of rescission, a period during which a borrower refinancing or taking a loan against a principal dwelling may cancel, a protection that does not apply to the loan used to purchase the home. The licensee should understand that the APR is the key comparison figure and that advertising rules constrain how loan terms may be promoted.

6.3 The Real Estate Settlement Procedures Act

The Real Estate Settlement Procedures Act, abbreviated RESPA, regulates the settlement, or closing, process for most residential mortgage loans. It has two broad thrusts. First, it requires disclosures that inform borrowers about settlement costs and the nature of the services they are paying for. Second, it prohibits practices that inflate those costs without benefit to the borrower, most notably kickbacks and referral fees among settlement-service providers. Under RESPA, a provider may not pay or receive a fee merely for referring business, because such payments raise costs and corrupt the borrower's interest in receiving services on the merits. RESPA also limits the amount a lender may require a borrower to deposit into an impound account for taxes and insurance, preventing lenders from holding excessive cushions of the borrower's money.

The anti-kickback prohibition is the part of RESPA most likely to touch a real estate licensee directly. Arrangements in which a settlement provider rewards an agent for steering clients to it can violate RESPA, and the licensee must be wary of any compensation that amounts to payment for a referral. The principle is that the borrower should receive settlement services chosen on their merits, not because someone was paid to steer the borrower.

6.4 The Integrated Disclosures: Loan Estimate and Closing Disclosure

For many years, TILA and RESPA disclosures were delivered on separate, overlapping forms that confused borrowers. Federal regulators integrated them into two clear forms that now govern most residential mortgage transactions, a reform often called by the shorthand of its rule combining the two laws.

The Loan Estimate is provided to the borrower shortly after application. It sets out, in a standardized format, the estimated interest rate, monthly payment, total closing costs, and key loan features, allowing the borrower to understand the proposed loan and to shop among lenders by comparing their Loan Estimates. It replaced the older early disclosure and good-faith estimate.

The Closing Disclosure is provided before closing and states the actual, final terms and costs of the loan. To give the borrower

time to review the final terms against the earlier estimate, the law requires that the Closing Disclosure be delivered a set number of business days before consummation, so the borrower is not confronted with surprises at the signing table. The two forms work as a pair: the Loan Estimate sets expectations early and enables comparison shopping, and the Closing Disclosure confirms the final deal with time to review. The licensee should understand the purpose and timing of each, because they structure the modern loan process and protect the borrower's ability to compare and to catch errors.

6.5 The Equal Credit Opportunity Act

The Equal Credit Opportunity Act, abbreviated ECOA, prohibits discrimination in any aspect of a credit transaction on the basis of protected characteristics, including race, color, religion, national origin, sex, marital status, age, and the fact that an applicant receives public assistance. Credit decisions must rest on the applicant's creditworthiness, the legitimate factors of capacity, credit history, and collateral, not on prohibited characteristics. ECOA also requires that an applicant denied credit receive notice of the action and, on request or automatically depending on the situation, a statement of the reasons, so that the applicant can understand and challenge the decision. ECOA is the lending counterpart of the fair-housing laws, and together they forbid discrimination across the housing and lending system.

6.6 The Home Mortgage Disclosure Act

The Home Mortgage Disclosure Act, abbreviated HMDA, requires many lenders to collect and publicly report data about the home loan applications they receive and the loans they make, including information about the applicants and the disposition of applications. The purpose is transparency: the data allow regulators and the public to detect patterns that may indicate discriminatory lending or the underserving of particular communities. HMDA does not by itself prohibit conduct; it shines a light on lending patterns so that problems such as redlining can be identified and addressed. The licensee should understand that lending is monitored through this reporting and that fair-lending compliance is observable in the aggregate data.

Worked Example: Comparing Two Loans by APR

A borrower receives two Loan Estimates for the same loan amount. The first loan has a note rate of 6.50 percent with high upfront fees and points; its APR is 6.95 percent. The second loan has a note rate of 6.75 percent with very low fees; its APR is 6.85 percent. The borrower is drawn to the first because its note rate is lower.

Guide the Analysis

The note rate alone is misleading, because the first loan's low rate is purchased with high upfront costs that the APR captures. The first loan's APR of 6.95 percent exceeds the second loan's APR of 6.85 percent, indicating that, over the life of the loan as the APR measures it, the first loan is actually the more expensive of the two despite its lower note rate. The borrower should also consider how long they expect to keep the loan, because heavy upfront costs are recovered only over time, but the APR comparison correctly signals that the second loan is cheaper on the standardized measure. The example shows precisely why TILA mandates the APR: it lets a borrower see past an attractive note rate to the true cost, which is the comparison the law exists to enable.

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7: Ethics, Fraud, Consumer Protection, and Fair Lending

7.1 Ethics in Lending

The people who arrange the largest debts of others' lives hold a position of trust, and ethical conduct is not optional decoration on top of the law but the foundation of a sustainable practice. The financial crisis of the late 2000s, driven in part by loans made without regard to whether borrowers could repay, demonstrated the social cost of unethical lending and prompted much of the regulation studied in the previous chapter. Ethics in lending means dealing honestly with borrowers, recommending loans suited to their circumstances, disclosing fully and accurately, avoiding conflicts of interest, and never profiting by exploiting a borrower's lack of information.

For a real estate licensee who arranges financing, ethical duties overlap with the fiduciary duties owed in agency and with the conduct standards of license law. The licensee must not steer a borrower into a costlier loan to earn a larger fee, must not misrepresent loan terms, and must not participate in arrangements that deceive lenders or borrowers. The reputation that sustains a career is built on the accumulation of honest transactions, and a single fraudulent or exploitative deal can end it.

7.2 Mortgage Fraud

Mortgage fraud is the intentional misrepresentation or omission of material information to obtain a loan or better loan terms than honest disclosure would yield. It takes many forms, and the licensee must recognize them in order to avoid both committing and facilitating them.

Fraud for housing is committed by a borrower who misrepresents information, such as income, employment, or the intent to occupy the property, in order to obtain a loan to buy a home the borrower could not otherwise finance. Fraud for profit is committed by industry insiders, sometimes in collusion, to extract money from a transaction, through schemes such as inflated appraisals, falsified documents, straw buyers who pose as the real purchaser, and property flipping at fraudulently inflated values. Income or asset misrepresentation, occupancy misrepresentation, and appraisal fraud are recurring elements.

Everyone is harmed by mortgage fraud. Lenders suffer losses, which raise costs for honest borrowers. Communities suffer when fraudulent loans lead to foreclosures. The borrower who participates in fraud, even at someone else's urging, faces serious legal consequences. A licensee who knowingly participates in or facilitates mortgage fraud commits a crime and forfeits the license. The duty is not only to refrain from fraud but to refuse to look away from it: signing or transmitting documents the licensee knows to be false is participation.

7.3 Predatory Lending

Predatory lending refers to lending practices that are abusive or unfair to the borrower, even when not always strictly fraudulent. Predatory practices include charging excessive fees and interest unrelated to the borrower's risk, making loans the borrower plainly cannot repay, repeatedly refinancing a loan to generate fees in a practice called loan flipping, packing loans with unnecessary products, imposing harsh prepayment penalties, and targeting vulnerable borrowers who do not understand the terms. Predatory lending often falls hardest on the elderly, the financially unsophisticated, and members of communities historically underserved by mainstream credit.

Much of the consumer-protection regulation studied earlier exists to curb predatory lending: the disclosure rules expose hidden costs, the limits on prepayment penalties reduce a common predatory tool, and the requirement to consider a borrower's ability to repay attacks the core abuse of lending without regard to repayment. The licensee should be able to recognize predatory features and should never steer a client toward a loan bearing them.

7.4 Fair Lending

Fair lending is the principle, enforced by law, that credit decisions must not discriminate on prohibited bases. The Equal Credit Opportunity Act, examined in the previous chapter, prohibits discrimination in credit on the basis of protected characteristics.

The Fair Housing Act prohibits discrimination in residential real estate financing as part of its broad prohibition on housing discrimination. Together they forbid discrimination across both the housing transaction and the loan that finances it.

Two prohibited practices deserve emphasis because they recur in lending. Redlining is the practice of denying or restricting credit in particular geographic areas, often defined by the racial or ethnic composition of the residents, regardless of the creditworthiness of individual applicants there. The term comes from the historical practice of outlining such areas in red on maps. Redlining is illegal because it bases credit decisions on the location and, implicitly, the protected characteristics of a community rather than on individual creditworthiness. Steering, in the lending context, includes directing borrowers toward or away from particular loan products or terms on a prohibited basis, such as channeling minority borrowers into costlier subprime loans for which their credit did not call. Both practices violate fair-lending law, and both have a documented history that the reporting required by the Home Mortgage Disclosure Act helps to detect.

The licensee's fair-lending duty is absolute and overrides any contrary instruction. A client's discriminatory preference does not excuse discriminatory conduct, because the duty of obedience extends only to lawful instructions. Treating all applicants equally on the merits of their creditworthiness is both a legal command and an ethical one.

7.5 Consumer Protection in Context

The consumer-protection framework around lending is broad and includes the federal disclosure laws, the fair-lending laws, the ability-to-repay requirements that emerged from the financial crisis, and the oversight of a federal consumer-protection agency that supervises mortgage lending and enforces many of these rules. The framework reflects a judgment that the mortgage market, left unchecked, can harm consumers and communities, and that disclosure, fair dealing, and accountability are necessary to a healthy lending system. The licensee operates inside this framework and serves clients best by understanding it, recognizing abuse, and conducting every transaction to a standard that the law and ethics both demand.

Worked Example: Spotting the Problem

A loan officer encourages a borrower to overstate income on the application, assuring the borrower that "everyone rounds up" and that it will help the loan close. The same officer offers a borrower in a particular neighborhood only a high-cost loan, though the borrower's credit would qualify for a standard one, and proposes refinancing another borrower for the third time in two years, generating fees each time.

Identify each Problem

Encouraging the borrower to overstate income is mortgage fraud, specifically income misrepresentation, and a licensee who participates commits a crime and risks the license regardless of who suggested it. Offering a borrower in a particular neighborhood only a high-cost loan despite qualifying credit suggests redlining or steering, prohibited fair-lending violations that base the loan offered on location rather than individual creditworthiness. Repeatedly refinancing to generate fees is loan flipping, a predatory practice. The example shows the three threats of this chapter, fraud, predatory lending, and discrimination, appearing in ordinary-looking conduct, and underscores that the licensee must recognize and refuse to participate in any of them.

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8: The Loan Process and Loan Documentation

8.1 The Loan Process as a Sequence

A residential mortgage moves through a recognizable sequence of stages, and understanding the sequence lets the licensee set expectations, anticipate problems, and explain to clients what happens next. The stages are application, processing, underwriting, approval with conditions, closing, and funding. Each produces documents and depends on the one before. A loan does not leap from application to funding; it advances through review, verification, and decision, and a delay or defect at any stage can stall the whole.

The process is also a record. Every loan generates a file documenting the borrower, the property, the terms, and the lender's decision, assembled so that the loan can be underwritten, sold into the secondary market, and audited later. The documents are not bureaucratic clutter; they are the evidence on which the lending decision rests and the basis on which the loan can be sold.

8.2 Application and the Uniform Residential Loan Application

The process begins when the borrower submits a loan application. The standard form is the Uniform Residential Loan Application, historically known by its form number as the 1003, the application used throughout the industry because it gathers the information the secondary market requires in a standardized way. The application collects the borrower's identity, employment and income, assets and liabilities, details of the property and the proposed loan, and declarations about the borrower's circumstances and intent, such as whether the borrower will occupy the property.

The application is the foundation of the file, and its accuracy is essential. Because the information drives the qualifying decision and because misrepresentation is fraud, the borrower and the originator share responsibility for ensuring the application is truthful and complete. Shortly after application, the lender must provide the Loan Estimate, the standardized early disclosure of the proposed terms and costs that lets the borrower compare offers, as the regulations chapter explained.

8.3 Processing: Assembling the File

In processing, the lender gathers and verifies the information needed to underwrite the loan. The borrower provides documentation of income, such as pay records and tax returns, and of assets, such as bank statements showing funds for the down payment and reserves. The lender pulls a credit report to review the borrower's credit history and obligations. The lender orders an appraisal to establish the value of the property that will secure the loan, and orders the title work and, where required, a preliminary title report. Verifications confirm employment and the source of funds. The processor assembles these items into a complete file ready for the underwriter's decision.

Processing is where many delays occur, because it depends on the borrower supplying documents promptly and on third parties, the appraiser, the title company, the employer, responding. A licensee who keeps a client moving through the documentation requirements helps the loan stay on schedule.

8.4 Underwriting: The Decision

Underwriting is the evaluation of the assembled file against the lender's and the secondary market's standards to decide whether to make the loan. The underwriter, or an automated underwriting system, weighs the borrower's capacity to repay, measured by income and the qualifying ratios developed in later chapters, the borrower's credit history, the funds available, and the value and condition of the property. Underwriting answers the central question of lending: will this borrower, on this property, on these terms, repay the loan, and is the collateral adequate if the borrower does not?

The decision is often not a simple yes or no but an approval with conditions. The underwriter may approve the loan subject to the borrower satisfying specified conditions, such as providing an additional document, explaining a deposit, paying off a particular debt, or correcting a defect in the title. The borrower clears the conditions, the file is updated, and the loan moves to closing. Understanding conditional approval helps the licensee reassure a client that conditions are routine and to be expected, not a

rejection.

8.5 Closing and the Closing Disclosure

Closing, also called settlement, is the stage at which the loan documents are signed and the transaction is consummated. Before closing, the lender must deliver the Closing Disclosure, the final standardized statement of the loan's actual terms and costs, a set number of business days in advance so the borrower can review the final deal against the earlier Loan Estimate. At closing, the borrower signs the promissory note and the security instrument, the deed of trust in California, along with the various disclosures and the closing documents. The borrower brings any funds required to close, and the escrow or settlement process, examined in the principles course, coordinates the exchange.

The signed deed of trust must be recorded to establish the lender's lien priority against third parties, which is why recording is part of the closing. The note evidences the debt, the deed of trust secures it, and recording protects the lender's position, the three working together exactly as the instruments chapter described.

8.6 Funding

Funding is the disbursement of the loan proceeds. After the documents are signed and, where required, any rescission period for a refinance has passed, the lender releases the funds, which flow through escrow to pay the seller and the costs of the transaction. With funding, the loan is complete: the borrower owns the home subject to the new deed of trust, the lender holds a recorded, secured loan, and the loan can now be sold into the secondary market and assigned to a servicer. The sequence that began with an application ends with a funded, recorded, salable loan.

Worked Example: Walking a Loan Through the Stages

A borrower applies for a loan to buy a home. Trace the file. At application, the borrower completes the uniform application and receives a Loan Estimate disclosing the proposed rate, payment, and costs. In processing, the borrower provides pay records, tax returns, and bank statements; the lender pulls credit, orders an appraisal that comes in at the contract price, and orders title work. In underwriting, the automated system and underwriter review the file and issue an approval conditioned on the borrower documenting the source of a recent large deposit and paying off a small outstanding debt. The borrower clears both conditions. Before closing, the lender delivers the Closing Disclosure showing the final terms, and after the required review period the borrower signs the note and the deed of trust. The deed of trust is recorded, the loan funds, and proceeds disburse through escrow to complete the purchase.

Notice how each stage produced its documents and depended on the prior stage, and how the disclosures, the appraisal, the title work, and the instruments all appeared at their proper points. The example assembles the chapter into a single coherent process and previews the qualifying detail that the next chapters supply.

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9: Conventional Financing

9.1 What a Conventional Loan Is

A conventional loan is a loan that is not insured or guaranteed by a government agency. The lender relies on the borrower's creditworthiness and on the property as collateral, without the backstop of FHA insurance or a VA guaranty. Conventional loans are the largest category of home loans, and the conventional conforming loan, one that also meets Fannie Mae and Freddie Mac standards, is the default product of the mortgage market. A conventional loan can be conforming or nonconforming; a jumbo loan, for instance, is conventional but non-conforming because it exceeds the conforming size limit.

The absence of government backing shapes the conventional loan's features. Because the lender bears the risk directly, the lender cares intensely about the down payment, the borrower's credit, and the ratios that measure risk, and it manages the risk of a small down payment through private mortgage insurance rather than government insurance. Conventional lending is, in this sense, the purest expression of the lender's own risk assessment.

9.2 The Down Payment and Loan-to-Value Ratio

The down payment is the portion of the purchase price the buyer pays in cash, and the loan covers the rest. The relationship between the loan and the value of the property is captured by the loan-to-value ratio, the single most important risk measure in mortgage lending. The loan-to-value ratio, abbreviated LTV, is the loan amount divided by the lesser of the purchase price or the appraised value, expressed as a percentage:

$$\text{LTV} = \frac{\text{Loan Amount}}{\text{Value}}$$

A larger down payment means a smaller loan relative to value, a lower LTV, and less risk to the lender, because the borrower has more equity at stake and the property is more likely to be worth at least the loan balance if values fall. A smaller down payment means a higher LTV and more risk. The LTV drives many lending decisions: the rate, the need for mortgage insurance, and sometimes whether the loan is made at all.

Worked Example: Loan-to-Value Ratio

A buyer purchases a home for $500,000 and makes a down payment of $100,000, borrowing $400,000. The appraisal equals the purchase price. The loan-to-value ratio is:

$$\begin{aligned}\text{LTV} &= \frac{\text{Loan Amount}}{\text{Value}} \\ &= \frac{\$400,000}{\$500,000} \\ &= 0.80 = 80\%\end{aligned}$$

The down payment of $100,000 is 20 percent of the price, the complement of the 80 percent LTV. Now suppose the appraisal had come in low, at $480,000, while the price remained $500,000. The LTV is calculated on the lesser of price or value, so the lender uses $480,000: the maximum loan at 80 percent LTV would be 0.80 times 480,000, which is $384,000, and the buyer would have to increase the down payment or renegotiate to bridge the gap. The example shows why the appraisal matters to the loan and why the LTV is computed on the lesser figure: the lender will not lend against value that the appraisal does not support.

Worked Example: Combined Loan-to-Value Ratio

When a property secures more than one loan, lenders measure risk by the combined loan-to-value ratio, abbreviated CLTV, which adds all the loans secured by the property and divides by the value.

A buyer purchases a $600,000 home with a first loan of $420,000 and a second loan of $60,000, putting $120,000 down. The CLTV is the sum of the loans divided by the value:

$$\begin{aligned} \text{LTV} &= \frac{\sum \text{Loan Amounts}}{\text{Value}} \\ &= \frac{\$420,000 + \$60,000}{\$600,000} \\ &= 0.80 = 80\% \end{aligned}$$

The first loan alone is a 70 percent LTV, but the combined financing reaches 80 percent. Lenders care about the CLTV because the total debt against the property, not just the first loan, determines the risk that a forced sale will fail to cover what is owed. The example shows why a borrower cannot evade the risk measures simply by splitting the financing into two loans; the combined ratio captures the full leverage.

9.3 Private Mortgage Insurance

When a conventional loan has a high LTV, typically above 80 percent, the lender faces greater risk and ordinarily requires private mortgage insurance, abbreviated PMI. Private mortgage insurance protects the lender, not the borrower, against loss if the borrower defaults and the foreclosure sale does not cover the loan. The borrower pays the premium, often as a monthly addition to the payment, until the requirement ends.

The requirement is tied to the LTV. As the borrower pays down the loan and as the property's value is established, the LTV falls, and federal law provides that PMI on many loans must be canceled when the loan balance reaches a specified percentage of the original value, and automatically terminated at a lower threshold, provided the borrower is current. PMI thus is not permanent; it covers the lender during the period of highest risk and ends as the borrower builds equity. The practical lesson for the borrower is that a down payment of 20 percent avoids PMI on a conventional loan, while a smaller down payment makes the home accessible sooner at the cost of paying PMI until enough equity accumulates. A knowledgeable licensee can explain this tradeoff clearly.

9.4 Fixed-Rate and Adjustable-Rate Conventional Loans

Conventional loans come in fixed-rate and adjustable-rate forms, and the choice allocates interestrate risk between borrower and lender.

A fixed-rate loan carries an interest rate that does not change for the life of the loan, so the principaland-interest payment is constant and predictable. The borrower is protected against rising rates, and the lender bears the risk that rates will rise above the fixed rate. The thirty-year fixed-rate loan is the archetypal American mortgage, valued for its stability.

An adjustable-rate loan, examined more fully in the chapter on alternative financing, carries a rate that adjusts periodically based on a published index, so the payment can rise or fall over time. The borrower accepts interest-rate risk in exchange for a lower initial rate. The fixed-rate loan trades a higher initial rate for certainty; the adjustable-rate loan trades certainty for a lower initial rate. The right choice depends on the borrower's expected time in the home, tolerance for payment risk, and view of where rates are heading, judgments a professional can help frame.

Worked Example: PMI and the Down Payment Decision

A buyer can afford a home priced at $400,000 and is deciding between a 20 percent down payment of $80,000, which avoids PMI, and a 10 percent down payment of $40,000, which preserves cash but requires PMI on the resulting 90 percent LTV loan.

Frame the Tradeoff

With 20 percent down, the loan is $320,000 at an 80 percent LTV, no PMI is required, and the monthly payment carries no insurance premium, but the buyer commits $80,000 in cash. With 10 percent down, the loan is $360,000 at a 90 percent LTV, the buyer keeps $40,000 in reserve, but pays PMI until the LTV falls to the cancellation threshold through paydown or appreciation. The buyer must weigh the cost of PMI over the period it will be paid against the value of keeping $40,000 available for reserves, repairs, or investment. There is no universally correct answer; a buyer short on cash may sensibly accept PMI to buy sooner, while a buyer with ample cash may prefer to avoid it. The example shows how the LTV, the PMI requirement, and the down payment decision interlock, and why explaining the tradeoff is part of competent service.

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10: Government Lending Programs

10.1 Government Backing of Loans

A government loan is one insured or guaranteed by a federal agency, in contrast to a conventional loan, which carries no such backing. The government does not, in these programs, lend the money itself; private lenders make the loans, and the government agency insures or guarantees them, reducing the lender's risk of loss. That reduced risk allows lenders to offer more lenient terms, such as smaller down payments and more flexible qualifying, than they would on a conventional loan, which serves the public purpose of expanding access to homeownership for borrowers who might not qualify conventionally. The three principal programs are the FHA-insured loan, the VA-guaranteed loan, and the USDA rural housing loan.

The distinction between insurance and a guaranty is worth noting. FHA insures loans, charging the borrower a premium that funds the insurance. The VA guarantees a portion of the loan, backed by the borrower's eligibility as a veteran rather than an insurance premium of the FHA kind, though the VA charges a funding fee. In both cases, the government's backing is what persuades the private lender to accept terms it would not accept on an unbacked conventional loan.

10.2 FHA-Insured Loans

The Federal Housing Administration, part of the Department of Housing and Urban Development, insures home loans made by approved lenders. The FHA insurance protects the lender against loss if the borrower defaults, which allows the FHA program to offer features attractive to borrowers with limited cash or imperfect credit. FHA loans are known for a low minimum down payment, more flexible credit qualifying than many conventional loans, and limits on the loan amount that vary by area.

The cost of FHA insurance is borne by the borrower in the form of mortgage insurance premiums. There is typically an upfront premium, which may be financed into the loan, and an annual premium paid monthly. Unlike conventional PMI, FHA mortgage insurance is structured differently and, depending on the loan terms and the era of the rules, may remain for much or all of the loan term rather than canceling automatically at a particular LTV. The licensee should understand that FHA insurance is a real and continuing cost, and that whether and when it ends depends on the program's current rules, which must be checked.

FHA loans serve borrowers who lack a large down payment or whose credit is too thin or imperfect for the best conventional terms. They are common among first-time buyers. The tradeoff is the ongoing insurance cost in exchange for accessibility.

10.3 VA-Guaranteed Loans

The Department of Veterans Affairs guarantees home loans made by private lenders to eligible veterans, active-duty service members, and certain surviving spouses. The VA guaranty, a promise to reimburse the lender for a portion of any loss, substitutes for the down payment and mortgage insurance that protect lenders on other loans, and it allows the program's signature benefit: eligible borrowers can often obtain a loan with no down payment.

VA loans carry several borrower-friendly features. The possibility of zero down payment is the most prominent. The VA does not require monthly mortgage insurance of the kind FHA and conventional high-LTV loans carry, though it charges a one-time funding fee, which may be financed and which is reduced or waived for certain borrowers such as those with service-connected disabilities. The VA also limits certain closing costs the veteran may pay and imposes its own appraisal, which establishes the property's value and confirms it meets minimum standards. Eligibility is established by the borrower's service record through a certificate of eligibility.

VA loans are a powerful benefit for those who qualify, frequently the most advantageous option available to an eligible veteran. The licensee working with veteran clients should ensure they know the benefit exists, because a veteran unaware of it might needlessly choose a costlier loan.

10.4 USDA Rural Housing Loans

The United States Department of Agriculture operates rural housing loan programs that support homeownership in eligible rural

and some suburban areas. These programs, through guaranties and in some cases direct loans, can offer no-down-payment financing to borrowers within income limits who buy in designated areas. The USDA program serves a different niche from FHA and VA: it is defined by geography and income rather than by the borrower's service or by a low down payment alone. The licensee should know the program exists and that its eligibility turns on the property's location in a designated area and on the borrower's income falling within limits, details that must be checked against current USDA designations and figures.

10.5 Comparing the Programs

The government programs are best understood by what each is for. FHA serves borrowers with limited down payment or imperfect credit, at the cost of ongoing mortgage insurance. VA serves eligible veterans and service members, often with no down payment and no monthly mortgage insurance, at the cost of a funding fee. USDA serves moderate-income borrowers in designated rural areas, often with no down payment. Conventional financing, by contrast, suits borrowers with stronger credit and a larger down payment who can avoid mortgage insurance and want the flexibility of the conventional market. Matching a borrower to the right program is a practical skill: a veteran with little cash should hear about the VA loan, a first-time buyer with a small down payment and fair credit should hear about FHA, a moderate-income buyer in a rural area should hear about USDA, and a well-qualified buyer with 20 percent down may do best conventionally. The professional who knows the menu can point each client toward the option that fits.

Worked Example: Matching Borrowers to Programs

Three buyers seek advice. The first is an honorably discharged veteran with steady income, good credit, and almost no cash for a down payment. The second is a first-time buyer with fair credit and enough saved for about 3.5 percent down. The third is a moderate-income family buying a home in a designated rural area with little cash.

Match Each

The veteran is an ideal candidate for a VA-guaranteed loan, which can offer no down payment and no monthly mortgage insurance, almost certainly the most advantageous option, so the licensee should make sure the veteran knows the benefit exists. The first-time buyer with fair credit and a small down payment fits the FHA-insured program, which accepts a low down payment and more flexible credit in exchange for mortgage insurance premiums. The moderate-income rural buyer should explore a USDA rural housing loan, which can offer no-down-payment financing to income-eligible buyers in designated areas. The example shows the payoff of knowing the programs: each buyer has a best-fit option, and identifying it can save the client substantial money and make a purchase possible that might otherwise not be.

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11: Alternative and Creative Financing

11.1 Beyond the Standard Loan

The fixed-rate, fully amortized loan is the backbone of residential finance, but it is not the only structure. A range of alternative arrangements adjusts the rate, the payment, the term, or the disbursement to fit particular needs and markets. These structures can lower an initial payment, finance construction, tap accumulated equity, or bridge a gap that standard financing cannot. They also carry risks that the standard loan avoids, and the licensee must understand both the uses and the dangers, because alternative financing has been at the center of past lending crises when its risks were ignored.

11.2 Adjustable-Rate Mortgages

An adjustable-rate mortgage, abbreviated ARM, carries an interest rate that changes periodically based on a published financial index, so the payment can rise or fall over the life of the loan. The ARM shifts interest-rate risk from the lender to the borrower, and in exchange the borrower usually receives a lower initial rate than a comparable fixed-rate loan.

An ARM has several components the borrower must understand. The index is the published rate to which the loan is tied; when the index moves, the loan's rate moves with it. The margin is a fixed percentage the lender adds to the index to set the loan's rate; the fully indexed rate is the index plus the margin. The initial rate, sometimes called a teaser rate, may be lower than the fully indexed rate for an introductory period, after which the rate adjusts to the fully indexed level. Adjustment periods set how often the rate changes. Caps limit how much the rate can change: a periodic cap limits the change at each adjustment, and a lifetime cap limits the total change over the life of the loan. A negative amortization feature, present in some risky ARMs, allows a payment so low that it does not cover the interest, so that the unpaid interest is added to the principal and the balance grows; this feature is dangerous and largely curtailed by post-crisis rules.

The borrower considering an ARM must look past the low initial rate to the fully indexed rate and the caps, because the payment can rise substantially when the introductory period ends. An ARM can serve a borrower who expects to sell or refinance before the rate adjusts, or who expects rates to fall, but it exposes a borrower who stays and faces rising rates to payment shock. The licensee should ensure a client understands the index, margin, caps, and the worst-case payment before choosing an ARM.

11.3 Interest-Only, Balloon, and Partially Amortized Loans

Several structures alter how principal is repaid. An interest-only loan requires payments of interest only for a period, with no reduction of principal during that time; payments are low, but the balance does not fall, and a larger payment or refinance looms when the interest-only period ends. A balloon loan requires regular payments that do not fully amortize the loan, leaving a large lumpsum balloon payment of the remaining principal due at maturity; the borrower must be prepared to pay, refinance, or sell when the balloon comes due. A partially amortized loan amortizes over a schedule longer than its actual term, so that regular payments reduce principal somewhat but a balloon remains at the end. These structures lower periodic payments at the cost of a future obligation, and they carry the risk that the borrower cannot meet the balloon or refinance on acceptable terms when the time comes, particularly if values or the borrower's circumstances have declined.

11.4 Construction Loans

A construction loan finances the building of improvements rather than the purchase of a completed property. It has distinctive features. The loan is typically short-term, covering the construction period, and the funds are disbursed in stages, called draws, as construction reaches specified milestones, rather than all at once, so the borrower pays interest only on the funds drawn. The lender inspects progress before releasing each draw, protecting itself against advancing money for work not done. Construction loans carry higher risk than loans on completed property, because a halfbuilt structure is poor collateral and construction can fail or run over budget, so they often carry higher rates and stricter terms. On completion, a construction loan is often replaced by permanent financing, sometimes arranged in advance as a combined construction-to-permanent loan. Because construction lenders insist on first-lien position, subordination of other financing is a common feature, connecting to the priority concepts studied earlier.

11.5 Open-End Loans and Equity Lines

An open-end loan allows the borrower to borrow additional sums in the future under the same security instrument, up to a limit, without taking out a wholly new loan. The home equity line of credit is the familiar example: a lender extends a revolving line secured by the borrower's home, and the borrower can draw, repay, and redraw up to the credit limit during a draw period. Open-end and equity financing let an owner tap accumulated equity for other purposes, but they encumber the home and, because they are usually junior to the first loan, carry the risks of junior financing and of converting home equity into debt. The licensee should understand that these are loans against the home, with the home at stake, however convenient the revolving access may appear.

11.6 Wraparound Financing and Buydowns

A wraparound loan, or all-inclusive trust deed, is a creative structure in which a new, larger loan from a seller or lender wraps around an existing loan that remains in place. The borrower makes one payment on the wraparound loan to the wraparound lender, who continues to pay the underlying existing loan and keeps the difference. Wraparounds can finance a sale when the existing loan carries a favorable rate, but they are complicated and risky: the underlying loan's due-on-sale clause may be triggered by the transfer, and the borrower depends on the wraparound lender to keep paying the underlying loan. Wraparounds require careful legal handling and full disclosure.

A buydown is an arrangement in which money is paid upfront to reduce the borrower's interest rate, either for the early years of the loan, a temporary buydown, or for its full life, a permanent buydown. A seller or builder may pay a buydown to make a property more affordable to the buyer, effectively lowering the buyer's initial payments. The cost of the buydown is paid at closing in exchange for the lower rate. Buydowns can help a buyer qualify or ease into payments, but the buyer should understand whether the reduced rate is temporary, in which case payments will rise, or permanent.

Worked Example: Reading an ARM

A borrower is offered a 5/1 ARM: the rate is fixed for the first five years, then adjusts annually. The initial rate is 5 percent. The loan is tied to an index currently at 4 percent with a margin of 2.5 percent, a periodic cap of 2 percent, and a lifetime cap of 5 percent above the initial rate.

Decode the loan

For the first five years the rate is 5 percent. After that, the rate adjusts to the fully indexed rate, the index plus the margin, currently 4 plus 2.5, which is 6.5 percent, higher than the 5 percent initial rate, so the payment would rise even if the index did not move, because the initial rate was a discounted teaser. At the first adjustment, the periodic cap of 2 percent limits the increase, so the rate could rise from 5 percent to at most 7 percent in that year. Over the life of the loan, the lifetime cap of 5 percent above the initial rate means the rate can never exceed 10 percent. The borrower should plan for the payment at the fully indexed rate and consider the worst case at the lifetime cap, not budget on the basis of the 5 percent teaser. The example shows why the components of an ARM matter: the initial rate alone badly understates the borrower's likely and possible future payments.

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12: Seller Financing and Junior Loans

12.1 When the Seller Becomes the Lender

Not all financing comes from institutions. In seller financing, also called owner financing or seller carryback, the seller extends credit to the buyer, accepting a promise to pay over time instead of receiving the full price in cash at closing. The seller, in effect, becomes a lender. Seller financing can make a transaction possible when institutional financing falls short, can give the seller an income stream and possible tax advantages on the spread-out gain, and can be quicker and more flexible than a bank loan. It also exposes the seller to the risk that the buyer will not pay, a risk a bank is equipped to manage and an individual seller often is not.

Seller financing appears in several forms. The seller may carry the entire purchase price, taking back a first loan, or may carry only part of it as a junior loan behind a new institutional first loan, a common way to bridge a gap in the buyer's financing. The instruments and the risks differ with the structure, and the licensee must understand them to advise either party.

12.2 The Purchase-Money Trust Deed

When a seller carries financing secured by the property sold, the instrument is typically a note and a deed of trust, often called a purchase-money trust deed because it secures money used to purchase the property. The buyer signs a note promising to pay the seller and a deed of trust pledging the property as security, exactly as with an institutional loan, but the beneficiary is the seller rather than a bank. The seller-carried loan can be a first deed of trust, if the seller carries the whole price, or a junior deed of trust behind an institutional first.

The purchase-money character carries legal significance studied in the default chapter: purchasemoney loans on owner-occupied homes enjoy anti-deficiency protection, meaning the lender, including a seller, is generally limited to the property on default and cannot pursue the buyer for a shortfall. A seller carrying financing should understand that this protection limits the seller's recourse, which is one of the risks of becoming a lender.

12.3 The Land Contract

A land contract, also called a contract for deed or an installment sales contract, is a distinctive sellerfinancing device in which the buyer takes possession and pays the purchase price in installments, but the seller retains legal title until the contract is paid in full. The buyer holds equitable title, the right to obtain legal title upon completing the payments, and enjoys possession and the benefits and burdens of ownership in the meantime, but does not hold legal title.

The land contract is attractive to a seller because retaining legal title appears to simplify recovery if the buyer defaults, and to a buyer who cannot obtain other financing. But it is risky, especially for the buyer. The buyer occupies and may improve a property to which the buyer does not hold legal title, and historically a defaulting buyer could lose both the property and the payments made. California law has added protections for buyers under land contracts, but the structure remains hazardous, and the licensee should ensure that a buyer entering a land contract understands that legal title remains with the seller until the contract is fully performed. Recording the land contract and using an escrow or third party to hold the deed and process payments can reduce some risks.

12.4 Junior Loans

A junior loan is any loan secured by the property that is subordinate in priority to a senior loan, typically a second deed of trust behind a first. Seller carrybacks are frequently junior, and so are home equity loans and lines. The junior position is defined by priority: in a forced sale, the junior lender is paid only after the senior lender is fully satisfied, so the junior lender bears more risk of loss if the sale proceeds fall short.

The greater risk of the junior position explains its features. Junior loans typically carry higher interest rates than senior loans, reflecting the added risk, and a junior lender pays close attention to the combined loan-to-value ratio, because the total debt

against the property determines how much cushion protects the junior position. A seller considering carrying a junior loan should understand that, behind a large first loan, the carryback may be poorly protected if values fall, and that the seller may receive little in a foreclosure by the senior lender. The licensee advising a seller-carryback should make this risk plain.

12.5 Risks to Seller and Buyer

Seller financing distributes risk to both parties, and a clear-eyed assessment serves both.

The seller's principal risk is nonpayment and the cost and limits of recovery. If the buyer defaults, the seller must foreclose, which takes time and money, and the anti-deficiency rules may limit the seller to the property. A seller who carries a junior loan behind a large first faces the additional risk of being wiped out in the senior lender's foreclosure. The seller should evaluate the buyer's creditworthiness much as a bank would, secure the loan properly, and consider the consequences of default before agreeing to carry financing.

The buyer's principal risks arise especially under land contracts, where legal title remains with the seller, and from the possibility that the seller has an underlying loan with a due-on-sale clause that the sale may trigger, or that the seller fails to pay an underlying loan, jeopardizing the buyer's interest. The buyer should confirm the state of the seller's title and any underlying loans, insist on proper instruments and recording, and use escrow to handle the transaction.

12.6 Disclosure in Seller-Financed Transactions

California requires disclosures designed to protect the parties in certain seller-financed residential transactions. A seller-financing disclosure statement informs the parties of the terms and risks of the arrangement, including the nature of the financing, the rights and obligations of the parties, and the consequences of default, so that neither party enters the arrangement without understanding it. The requirement reflects the recognition that seller financing, though useful, is complex and risky, and that parties who are not professional lenders need clear information. The licensee arranging a seller-financed transaction must ensure the required disclosures are made and should encourage both parties to obtain professional advice, because the structure carries legal and tax consequences that exceed what a survey course can fully address.

Worked Example: Structuring a Seller Carryback

A buyer can obtain an institutional first loan for 80 percent of a $500,000 purchase price, which is $400,000, and has a $50,000 down payment, leaving a $50,000 gap. The seller is willing to carry a second loan for the $50,000 to make the sale happen.

Analyze the Structure

The institutional first loan of $400,000 is the senior lien at an 80 percent loanto-value ratio. The seller's $50,000 carryback is a junior second loan, and the buyer's $50,000 down payment covers the remaining 10 percent. The combined loan-to-value ratio is the two loans divided by the price: 450,000 divided by 500,000, which is 90 percent. The seller, in the junior position behind a $400,000 first, bears real risk: if the buyer defaults and the first lender forecloses when values have fallen, the seller's $50,000 second could be partly or wholly lost, because the junior is paid only after the senior is satisfied. The seller should weigh that risk, evaluate the buyer's creditworthiness, ensure proper instruments and recording, and make the required disclosures. The example shows seller financing doing useful work, bridging a financing gap, while exposing the seller to the junior-position risk that the licensee must explain.

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13: Qualifying the Borrower- Income, Credit, and Ratios

13.1 What Qualifying Means

Qualifying the borrower is the process of determining whether a borrower can be expected to repay a loan. It is the heart of underwriting and the daily work of lending. A lender evaluating a borrower is asking, in effect, whether the borrower has the income to make the payments, the history of paying debts responsibly, and the assets to complete the purchase and weather setbacks. These concerns are traditionally summarized as the three Cs: capacity, credit, and collateral. Capacity is the borrower's ability to repay from income; credit is the borrower's record of repaying obligations; collateral is the property securing the loan, addressed in the next chapter. This chapter develops the borrower side, capacity and credit, with the quantitative methods the broker examination tests.

13.2 Capacity and the Qualifying Ratios

Capacity is measured chiefly through qualifying ratios that compare the borrower's obligations to income. Two ratios are central, and the licensee preparing for the broker examination must be able to calculate both.

The front-end ratio, also called the housing ratio, compares the proposed monthly housing payment to the borrower's gross monthly income. The housing payment for this purpose is often abbreviated PITI, for principal, interest, taxes, and insurance, and includes any homeowners-association dues and mortgage insurance. The front-end ratio is:

$$\text{Front-end ratio} = \frac{\text{Housing Payment (PITI)}}{\text{Gross Monthly Income}}$$

The back-end ratio, also called the total debt ratio, compares the housing payment plus all other recurring monthly debt obligations, such as car loans, student loans, and minimum credit card payments, to gross monthly income:

$$\text{Back-end ratio} = \frac{\text{Housing Payment} + \text{Other Monthly Debts}}{\text{Gross Monthly Income}}$$

Lenders set maximum allowable ratios, which vary by loan program and the strength of the overall file. A common illustrative standard for conventional loans is a front-end limit around 28 percent and a back-end limit around 36 percent, often expressed as 28/36, though many loans allow higher ratios with compensating strengths such as excellent credit or large reserves, and government programs use their own limits. The licensee should treat specific limits as program-dependent and verify them, while mastering the calculation itself, which does not change.

Worked Example: Calculating the Qualifying Ratios

A borrower has gross monthly income of $8,000. The proposed housing payment, PITI, is $2,000. The borrower also has a car payment of $400 and student loan and credit card minimums totaling $300, for other monthly debts of $700.

Calculate the front-end ratio

The housing payment divided by gross income, which is 2,000 divided by 8,000, equal to 0.25, or 25 percent. Calculate the back-end ratio: the housing payment plus other debts divided by gross income, which is (2,000 plus 700) divided by 8,000, equal to 2,700 divided by 8,000, which is 0.3375, or about 33.8 percent.

Compare to an illustrative 28/36 standard. The front-end ratio of 25 percent is within the 28 percent limit, and the back-end ratio of about 33.8 percent is within the 36 percent limit, so the borrower qualifies on both ratios under this standard. The example shows the core qualifying calculation: compute each ratio and compare it to the program's limit, with the back-end ratio usually the binding constraint because it captures all the borrower's debt.

Worked Example: Maximum Payment and Loan Amount

The ratios can be run in reverse to find the maximum housing payment, and hence the maximum loan, a borrower qualifies for. This is the calculation a licensee uses to tell a client what they can afford.

Take a borrower with gross monthly income of $9,000 and other monthly debts of $500, under a 28/36 standard. The front-end limit allows a housing payment up to 28 percent of income: 9,000 times 0.28, which is $2,520. The back-end limit allows total debt up to 36 percent of income: 9,000 times 0.36, which is $3,240; subtracting the $500 of other debts leaves $2,740 available for housing. The binding limit is the lower of the two, so the maximum housing payment is $2,520, set by the front-end ratio here.

To translate the $2,520 housing payment into a loan amount, the licensee subtracts the portions for taxes, insurance, and any mortgage insurance and association dues to find the amount available for principal and interest, then uses the payment-to-loan relationship developed in the mathematics chapter to find the supportable loan. If taxes, insurance, and dues come to $520 per month, then $2,000 is available for principal and interest, and at a given rate and term that payment supports a specific loan amount. The example shows the practical power of the ratios: run forward they test a proposed loan, and run backward they tell a borrower the ceiling on what they can borrow and buy.

13.3 Credit

Credit is the borrower's record of repaying obligations, and it is evaluated through credit reports and credit scores. A credit report compiles the borrower's accounts, payment history, balances, and any derogatory items such as late payments, collections, judgments, or bankruptcy. A credit score is a number summarizing the borrower's credit risk derived from the report, with higher scores indicating lower risk. Lenders use the score and the report together: the score gives a quick measure of risk, and the report reveals the detail behind it.

Credit affects qualifying in several ways. A higher score can qualify a borrower for a lower interest rate and more favorable terms, because the lender prices the loan to the risk; a lower score can raise the rate, require a larger down payment, or disqualify the borrower from certain programs. Derogatory items can bar or delay qualifying, sometimes for a defined period after a bankruptcy or foreclosure. Because credit so directly affects both qualifying and pricing, a borrower preparing to buy benefits from reviewing and improving credit in advance, and a licensee can helpfully encourage a client to check their credit early, while never advising anything that misrepresents the borrower's true situation.

13.4 Income and Asset Documentation and Reserves

Capacity rests on income that is documented and stable. Lenders verify income through documentation appropriate to its source: pay records and employment verification for wage earners, and tax returns and business records for the self-employed, whose income is often averaged over time and adjusted for the variability and deductions of self-employment. Income must generally be stable and likely to continue; a temporary or unverifiable income stream may not count.

Assets are documented to confirm that the borrower has the funds to close, the down payment and closing costs, and often reserves, additional funds remaining after closing to cover several months of payments in case of a setback. Lenders verify assets through bank and investment statements and scrutinize large or recent deposits to confirm they are not undisclosed loans, which would add to the borrower's debt. The documentation of income and assets is where the qualifying decision is grounded in evidence, and it connects to the loan process chapter, where assembling and verifying this documentation is the work of processing. A borrower who supplies clean, complete documentation moves smoothly through qualifying; gaps and unexplained items create the conditions that delay approval.

Worked Example: Putting Qualifying Together

A borrower earns $7,500 gross per month, has a car payment of $350 and other debt minimums of $250, a good credit score, and enough verified savings for the down payment plus several months of reserves. The proposed housing payment is $1,950.

Assess the File

The front-end ratio is 1,950 divided by 7,500, which is 0.26, or 26 percent, within an illustrative 28 percent limit. The back-end ratio is (1,950 plus 600) divided by 7,500, which is 2,550 divided by 7,500, equal to 0.34, or 34 percent, within an illustrative 36 percent limit. The good credit score supports favorable pricing and signals low risk. The verified down payment and reserves satisfy the asset requirement and strengthen the file. On capacity and credit, this borrower qualifies comfortably, and the documented reserves provide a compensating strength that could support flexibility if needed. The example assembles the chapter: ratios for capacity, the score and report for credit, and documented funds for assets, the three together forming the borrower side of the underwriting decision.

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14: Qualifying the Property- Appraisal and Underwriting

14.1 Why the Property Must Qualify Too

A loan is secured by the property, and if the borrower defaults the lender must look to the property to recover the debt. The lender therefore qualifies not only the borrower but the collateral, asking whether the property is worth enough, and is sound enough, to secure the loan. This is the third of the three Cs, collateral, and it is as essential as capacity and credit, because even a creditworthy borrower's loan is unsafe if the property does not support it. Qualifying the property is accomplished principally through the appraisal, supported by the lender's review of the property's condition, title, and characteristics.

The borrower side and the property side meet in the loan-to-value ratio. The borrower's down payment and the property's value together determine the LTV, and the LTV determines much about the loan. A low appraisal raises the effective LTV or shrinks the loan the lender will make, which is why the appraisal is one of the most consequential events in the loan process.

14.2 The Appraisal in Lending

An appraisal is an independent, impartial estimate of the property's market value, prepared by a licensed or certified appraiser. The lender orders the appraisal to confirm that the collateral is worth at least enough to secure the loan, and federal rules require the appraiser's independence so that the value reflects professional judgment rather than pressure to reach the price the parties agreed. The appraisal protects the lender, and indirectly the secondary-market investor who will own the loan, against lending more than the property is worth.

The appraiser uses the three approaches to value developed in the principles course, selecting and weighting them by the property type. The sales comparison approach, which adjusts the prices of comparable recent sales to the subject, is primary for typical homes, and it is the approach a lender most relies on for residential collateral. The cost approach, replacement cost less depreciation plus land, serves new or special-purpose properties. The income approach, capitalizing the property's net operating income, is primary for income property. For a standard home loan, the lender expects an appraisal grounded in comparable sales that supports the contract price.

Worked Example: Appraisal, LTV, and Loan Amount

A buyer agrees to pay $500,000 for a home and seeks an 80 percent loan, expecting to borrow $400,000 with $100,000 down. The appraisal, however, comes in at $480,000.

Work the Consequence

The loan-to-value ratio is computed on the lesser of the purchase price or the appraised value, so the lender uses the $480,000 appraised value, not the $500,000 price. An 80 percent loan on $480,000 is 0.80 times 480,000, which is $384,000, not the $400,000 the buyer expected. The buyer faces a $16,000 gap. The buyer can cover the gap with additional cash, raising the down payment to $116,000; can attempt to renegotiate the price down toward the appraised value; can challenge the appraisal with additional comparable sales if the appraisal appears flawed; or, if a purchase contract appraisal contingency allows, can cancel. The example shows the direct mechanical link between the appraisal and the loan: because the LTV is figured on the lesser of price or value, a low appraisal reduces the loan and forces a decision, which is why the appraisal is so consequential.

14.4 Beyond Value: Condition and Characteristics

The lender's interest in the property extends beyond its dollar value to its condition and characteristics, because these affect both the value and the property's adequacy as collateral. The appraisal notes the property's condition, and significant defects, a failing roof, structural problems, health and safety hazards, can require repair before the loan closes, particularly on government loans, which impose minimum property standards. The lender confirms that the property is a type it will lend on; some property types, conditions, or uses fall outside a given program. The lender also relies on the title work to confirm that the property's title is clear

enough to secure the loan, connecting to the title and escrow material of the principles course. A property that appraises well but has a clouded title or a serious physical defect may still fail to qualify until the problem is resolved.

For government loans, the property standards are more demanding. FHA and VA appraisals assess not only value but whether the property meets minimum standards of safety, soundness, and security, and a property that fails may require repairs before the loan can proceed. The licensee should anticipate that a government-financed purchase may surface property conditions that must be addressed, and should prepare clients accordingly.

14.5 How a Low Appraisal Plays Out

Because the low appraisal is so common and so disruptive, the licensee should understand the dynamics. When an appraisal comes in below the contract price, the financing premise of the deal is disturbed, because the lender will lend only against the appraised value. The parties then negotiate within the options the situation creates: the buyer brings more cash, the seller lowers the price, the parties split the difference, the appraisal is challenged, or the deal is canceled under a contingency. The outcome depends on the strength of each party's position, the market, and the terms of the purchase contract. A licensee who understands the appraisal's role can prepare clients for the possibility, advise on responses, and keep a transaction alive that a less informed party might let collapse. The low appraisal is not a dead end; it is a problem with several known solutions, and guiding clients through them is part of competent service.

Worked Example: Responding to a Low Appraisal

A seller and buyer are in contract at $620,000. The appraisal returns at $600,000. The buyer planned to put 20 percent down and finance 80 percent. The buyer has limited additional cash, and the market is balanced, with neither party holding overwhelming leverage.

Reason through the Responses

At the contract price, an 80 percent loan would have been 0.80 times 620,000, which is $496,000, with $124,000 down. But the loan is figured on the lower appraised value of $600,000, so an 80 percent loan is now 0.80 times 600,000, which is $480,000. To keep the same 80 percent financing against the appraised value and still buy at $620,000, the buyer would need $140,000 down, $16,000 more than planned, which the buyer cannot easily produce. The realistic options are to ask the seller to reduce the price toward $600,000, to split the $20,000 gap so each side gives somewhat, to challenge the appraisal if better comparables exist, or, failing agreement, to cancel under the appraisal contingency. In a balanced market the parties often meet in the middle. The example shows the licensee turning a disruptive appraisal into a structured negotiation with known options, the practical skill this chapter aims to build.

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15: Real Estate Finance Mathematics

15.1 Why a Mathematics Chapter

Finance mathematics has appeared throughout this book, worked where each concept arose. This chapter gathers the calculations in one place, develops the amortization relationships the broker examination tests most rigorously, and provides a reference for practice. The examination rewards fluency, the ability to identify which relationship a problem calls for and to apply it quickly and accurately, and fluency comes only from working many problems. Treat this chapter as a workbook: read each method, then work its examples until the procedure is automatic.

A note on tools. The amortization relationship between a loan, its rate, its term, and its payment involves compounding and is calculated with a financial calculator or an amortization factor table rather than by simple arithmetic. This chapter shows the structure of each calculation and uses representative factors so the method is clear; in practice the licensee uses a financial calculator or the lender's software. What the examination tests is whether you know which quantity to solve for and how the quantities relate, not whether you can compute a compound factor by hand.

15.2 Simple Interest

Simple interest is the foundation, introduced in the first chapter and repeated here for completeness. The relationship is interest equals principal times rate times time:

$$I = P \times R \times T$$

Any one of the four quantities can be found from the other three by rearrangement. To find the principal, divide interest by the product of rate and time. To find the rate, divide interest by the product of principal and time. To find the time, divide interest by the product of principal and rate.

Worked Example

A loan of $200,000 at an annual rate of 6 percent accrues, in one year, interest of 200,000 times 0.06 times 1, which is $12,000; in one month, that is 12,000 divided by 12, which is $1,000. Reverse it: if a one-month interest charge is $1,000 at a 6 percent annual rate, the monthly rate is 0.06 divided by 12, which is 0.005, and the principal is 1,000 divided by 0.005, which is $200,000. Practicing the rearrangement until it is automatic answers a whole class of examination problems.

15.3 Amortization: Payment, Rate, and Term

An amortized loan is repaid in equal periodic payments that cover the interest due each period and gradually retire the principal, so the balance reaches zero at the end of the term. Early payments are mostly interest, because the balance is large; later payments are mostly principal, because the balance has shrunk. The four quantities of an amortized loan are the loan amount, the interest rate, the term, and the payment, and they are linked so that, given any three, the fourth is determined. The Huber course objective states this directly: find the payment given loan, rate, and term; find the rate given loan, payment, and term; find the term given loan, rate, and payment.

The payment is calculated using an amortization factor, the monthly payment per dollar (or per thousand dollars) of loan at a given rate and term. The payment is the loan amount times the factor:

$$\text{Payment} = \text{Loan Amount} \times \text{Factor}(\text{rate},\text{term})$$

Worked Example: Finding the Payment

Suppose the factor for a 30-year loan at 6 percent is about $5.9955 per $1,000 borrowed, a representative figure from an amortization table. For a $300,000 loan, the number of thousands is 300, so the monthly principal-and-interest payment is 300 times 5.9955, which is about $1,799. This is the calculation a licensee runs to tell a borrower the payment on a contemplated loan, and it is the forward direction of the amortization relationship.

Worked example, finding the loan from the payment. The relationship reverses to find how large a loan a given payment supports, the calculation used in qualifying. If a borrower can pay $1,799 per month toward principal and interest at the same rate and term, divide the payment by the factor and multiply by a thousand: 1,799 divided by 5.9955 is about 300 thousands, so about $300,000. This is how the maximum housing payment from the qualifying chapter becomes a maximum loan amount.

Worked Example: Finding the Rate or the Term

If the loan and payment are known, the factor is the payment divided by the number of thousands, and the rate is the rate that produces that factor for the term, found from the table or the calculator. Finding the term works the same way: with the loan, rate, and payment known, the term is the one that makes the numbers reconcile. The examination may give three quantities and ask for the fourth in any of these directions, so the licensee must recognize which is missing and use the relationship accordingly. The conceptual point, more important than any single factor, is that loan, rate, term, and payment form one system: change any one and another must change to keep the loan amortizing to zero.

15.4 The Interest-and-Principal Split of a Payment

Within an amortized payment, the interest portion is the periodic rate times the current balance, and the rest reduces principal. This explains the amortization pattern and appears on examinations.

Worked Example

On a $300,000 loan at 6 percent annual, the first month's interest is the monthly rate times the balance: 0.06 divided by 12 is 0.005, times 300,000 is $1,500. If the payment is $1,799, then $1,500 is interest and the remaining $299 reduces principal, leaving a balance of $299,701. The next month's interest is 0.005 times 299,701, which is about $1,498.51, slightly less, so slightly more of the payment goes to principal. Repeating this is exactly what an amortization schedule does, and it shows why early payments are mostly interest and why paying extra principal early saves substantial interest over the loan's life.

15.5 Loan-to-Value and Combined Loan-to-Value

The loan-to-value ratio is the loan amount divided by the lesser of price or appraised value, and the combined loan-to-value ratio is all loans against the property divided by value. These were worked in the conventional financing chapter and are summarized here.

Worked Example

A $450,000 loan on a home priced at $600,000 and appraised at value has an LTV of 450,000 divided by 600,000, which is 0.75, or 75 percent. If a second loan of $30,000 is added, the CLTV is 480,000 divided by 600,000, which is 0.80, or 80 percent. To find the maximum loan at a target LTV, multiply the value by the LTV: at 80 percent of $600,000, the maximum first loan is $480,000. When the appraisal is below the price, use the lower appraised value as the denominator and the basis for the maximum loan, as the property-qualifying chapter showed.

15.6 Points

A point is one percent of the loan amount, charged by the lender as an upfront fee. Discount points are paid to reduce the interest rate; an origination point compensates the lender for making the loan. Because a point is one percent of the loan, its dollar cost is straightforward.

Worked Example

On a $400,000 loan, one point is one percent of 400,000, which is $4,000; two and a half points are 0.025 times 400,000, which is $10,000. Points increase the lender's yield, the effective return on the loan, because the lender advances less net cash, the loan amount minus the points, while collecting payments on the full face amount. Points also figure into the annual percentage rate, because they are a finance charge. The examination tests both the dollar cost of points, simple percentage arithmetic, and the understanding that points paid to reduce the rate are a tradeoff: cash now for a lower payment over time, worthwhile only if the borrower keeps the loan long enough to recover the upfront cost.

15.7 Qualifying Ratios

The front-end ratio is the housing payment divided by gross monthly income; the back-end ratio is the housing payment plus other monthly debts divided by gross monthly income. These were developed in the borrower-qualifying chapter; the calculation is summarized here for the math reference.

Worked Example

With gross monthly income of $8,000, a housing payment of $2,000, and other debts of $700: the front-end ratio is 2,000 divided by 8,000, which is 25 percent; the back-end ratio is 2,700 divided by 8,000, which is about 33.75 percent. Run in reverse under a 28/36 standard: the maximum housing payment is 0.28 times 8,000, which is $2,240, and the maximum total debt is 0.36 times 8,000, which is $2,880, leaving 2,880 minus 700, which is $2,180 for housing; the binding limit is the lower, $2,180. That housing figure, less taxes and insurance, becomes the principal-and-interest payment, which the amortization relationship converts to a maximum loan.

15.8 Prorations

Proration divides a continuing expense or income, such as property taxes, insurance, or interest, between buyer and seller as of the closing date, so each pays for the period of ownership. The method computes a daily amount and multiplies by the number of days each party owns.

Worked Example

Annual property taxes of $7,300 produce a daily amount of 7,300 divided by 365, which is $20 per day. If the seller owned the property for 120 days of the period for which taxes are owed at closing, the seller's share is 20 times 120, which is $2,400, and the buyer is responsible for the remainder. Interest on a loan is prorated similarly using the daily interest on the balance. The examination tests prorations as careful arithmetic: find the daily rate, count the days correctly, and assign each party its share.

15.9 The Annual Percentage Rate

The annual percentage rate expresses the cost of credit as a yearly rate that includes the note interest and certain finance charges, such as points and some fees, spread over the loan. Because it captures more than the note rate, the APR is usually higher than the note rate, and it is the figure the Truth in Lending Act requires for comparison. The APR itself is computed by a standardized method, in practice by the lender's software, and the examination tests the concept, that the APR includes finance charges beyond the note rate and therefore exceeds it, and that comparing APRs compares true costs, rather than asking the

candidate to compute the APR by hand.

15.10 Worked Example: A Combined Problem

A borrower with $9,000 gross monthly income and $600 in other monthly debts is buying a $500,000 home, putting 20 percent down, and financing the rest at a 30-year rate whose amortization factor is about $5.9955 per $1,000. Taxes and insurance are $500 per month. The lender uses a 28/36 standard and charges two points.

Work it Through

The down payment is 0.20 times 500,000, which is $100,000, so the loan is $400,000, an 80 percent LTV. The monthly principal-and-interest payment is 400 times 5.9955, which is about $2,398. Adding $500 of taxes and insurance gives a housing payment of about $2,898. Test the ratios: the front-end ratio is 2,898 divided by 9,000, which is about 32.2 percent, above the 28 percent guideline; the back-end ratio is (2,898 plus 600) divided by 9,000, which is about 38.9 percent, above the 36 percent guideline. So this borrower, on these guidelines, does not qualify for this loan without compensating strengths, a larger down payment, or a less expensive home. The two points cost 0.02 times 400,000, which is $8,000 at closing. The example chains the chapter's methods, down payment and LTV, the amortization factor for the payment, the qualifying ratios, and points, into the kind of multi-step problem the broker examination and real practice both demand.

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16: Default, Foreclosure, and the Anatomy of a Financed Transaction

16.1 When Repayment Fails

Most loans are repaid, but finance must account for the loans that are not, because the lender's willingness to lend depends on its ability to recover when a borrower defaults. Default is the borrower's failure to meet the obligations of the loan, most commonly by failing to make payments, though it can also arise from failing to pay taxes or insurance, or from other breaches of the loan terms. When default occurs, the security instrument gives the lender remedies, and understanding them completes the picture of how a secured loan works. This capstone chapter first develops default and foreclosure, then assembles the entire book into the story of one financed transaction.

16.2 The Lender's Response to Default

A lender facing default does not immediately seize the property. The process typically begins with notices and an opportunity for the borrower to cure the default by bringing the loan current. If the default is not cured, the acceleration clause studied in the instruments chapter allows the lender to declare the entire unpaid balance due, which is the predicate for foreclosure, because the lender forecloses to recover the full accelerated debt rather than only the missed payments. Throughout, the borrower may have opportunities to reinstate the loan or to pursue alternatives short of foreclosure. The lender generally prefers to be repaid rather than to own real estate, so workouts and alternatives are common, but the ultimate remedy, foreclosure, is what gives the security its force.

16.3 Judicial and Nonjudicial Foreclosure

Foreclosure is the process by which the lender forces a sale of the secured property to satisfy the debt, and it comes in two forms whose distinction is central to California finance.

Judicial foreclosure is a court-supervised lawsuit. The lender sues, obtains a judgment, and the property is sold under the court's authority. Judicial foreclosure is slower and more expensive, but it can, in some circumstances, allow the lender to pursue a deficiency judgment for a shortfall and it is associated with a statutory right of redemption after the sale. It is used in California in particular situations but is not the common path.

Nonjudicial foreclosure proceeds under the power of sale contained in the deed of trust, without a lawsuit. Because the trustor granted the trustee the power to sell on default, the trustee can conduct the sale after following the statutory notice procedure: recording a notice of default, allowing a statutory cure period, and then giving notice of sale before selling the property at a public auction called a trustee's sale. Nonjudicial foreclosure is faster and cheaper than judicial foreclosure, which is why the deed of trust and its power of sale dominate California lending. The tradeoff for the lender is that nonjudicial foreclosure generally forecloses the possibility of a deficiency judgment, and it does not carry the post-sale redemption right associated with judicial foreclosure.

16.4 Anti-Deficiency Protection and Redemption

California law limits a lender's recovery in important ways that the licensee must understand.

A deficiency is the shortfall when a foreclosure sale brings less than the debt owed. A deficiency judgment is a judgment against the borrower personally for that shortfall. California restricts deficiency judgments significantly. Purchase-money loans on owner-occupied residences of limited size are protected, meaning the lender is generally limited to the property and cannot pursue the borrower for a deficiency, a protection that extends to seller carrybacks securing the purchase price. And because nonjudicial foreclosure under the power of sale generally bars a deficiency judgment, the path most lenders choose itself limits recovery to the property. These rules shift risk onto lenders and protect borrowers from being pursued after losing the home, and they are a recurring subject on the examination.

Redemption is the borrower's right to recover the property by paying what is owed. A right of reinstatement allows the borrower to cure the default and stop the foreclosure during the statutory period before sale. A statutory right of redemption after the sale exists in judicial foreclosure but not in the typical nonjudicial trustee's sale, another reason the two paths differ in their consequences. The interplay of foreclosure method, deficiency rules, and redemption rights explains why the choice between judicial and nonjudicial foreclosure is consequential for both parties.

16.5 Alternatives to Foreclosure

Because foreclosure is costly to everyone, alternatives are common. In a deed in lieu of foreclosure, the borrower voluntarily conveys the property to the lender to satisfy the debt, avoiding the foreclosure process, though the lender accepts the property subject to junior liens and must weigh that. In a short sale, the lender agrees to let the borrower sell the property for less than the loan balance and accepts the proceeds in satisfaction, which can be less damaging to the borrower and less costly to the lender than foreclosure. Loan modifications and forbearance adjust the terms or pause payments to help a borrower through a temporary hardship. These alternatives reflect the reality that a negotiated resolution often serves both parties better than a forced sale, and the licensee may encounter them when working with distressed owners. Each carries legal and tax consequences that warrant professional advice.

16.6 The Anatomy of a Financed Transaction

The book closes by tracing a single financed purchase from beginning to end, naming every role and showing how the chapters connect. Follow one loan.

A buyer finds a home and applies for a loan. A mortgage loan originator, licensed under the SAFE

Act and holding a unique identifier, takes the application on the uniform residential loan application and provides the Loan Estimate required by the integrated disclosures. This is the environment, the markets, the SAFE Act, the loan process, and the regulations chapters at work in the opening minutes of the deal.

The lender, a primary-market institution that intends to sell the loan, sends the file to processing. A processor gathers the borrower's income and asset documentation, orders a credit report, orders an appraisal, and orders the title work. The appraiser, independent as the rules require, values the property as collateral. The title company examines title. This is processing, qualifying the borrower through capacity and credit, and qualifying the property through the appraisal.

An underwriter, or an automated underwriting system encoding secondary-market standards, evaluates the file: the qualifying ratios measure capacity, the credit report and score measure credit, the appraisal and loan-to-value ratio measure collateral. The underwriter issues an approval with conditions. The borrower clears the conditions. This is underwriting and the three Cs, with the finance mathematics determining the payment, the ratios, and the LTV.

Before closing, the lender delivers the Closing Disclosure with its required review period. At closing, the borrower signs the promissory note, the debt, and the deed of trust, the security, naming a trustee and the lender as beneficiary, with its acceleration, due-on-sale, and power-of-sale clauses. The deed of trust is recorded to establish lien priority. This is the instruments chapter and the closing stage.

The loan funds; proceeds disburse through escrow to the seller. The lender then sells the loan into the secondary market to an agency or investor, recovering capital to lend again, and the loan is assigned to a servicer who will collect the payments. This is the primary and secondary markets and servicing.

For years the borrower pays, each payment splitting into interest on the balance and principal, the amortization of the mathematics chapter. Suppose the borrower later falls into default. The servicer issues notices; the borrower cannot cure; the beneficiary accelerates and the trustee begins a nonjudicial foreclosure under the power of sale, recording a notice of default, allowing the cure period, and noticing a trustee's sale. Because the loan was a purchase-money loan on the borrower's home foreclosed nonjudicially, the lender is limited to the property and cannot pursue the borrower for a deficiency. Alternatively, the borrower and lender might have resolved the hardship through a short sale or a deed in lieu. This is the default and foreclosure material that completes the loan's life.

Every chapter of the book appears in this single transaction. The environment set the rate; the markets supplied and resold the funds; the SAFE Act licensed the originator; the instruments created and secured the debt; the regulations governed the

disclosures; ethics and fair lending constrained the conduct; the loan process sequenced the work; the products defined the loan; qualifying the borrower and the property made the decision; the mathematics quantified it; and default and foreclosure stood ready if repayment failed. Finance is a system, and the anatomy of one transaction is the system in motion.

16.7 Worked Example: Naming the Roles

In the transaction above, list the parties and the role each plays: the borrower, who promises to repay and pledges the property; the mortgage loan originator, who takes the application and discloses; the processor, who assembles the file; the appraiser, who values the collateral; the title company, who examines title; the underwriter, who decides; the lender or beneficiary, who funds and holds the loan until sale; the trustee, who holds power of sale under the deed of trust; the escrow holder, who coordinates the closing and disburses; the secondary-market investor, who buys the loan; and the servicer, who collects payments and manages any default. Naming each role and stating its function is a frequent examination task and the clearest summary of how a financed transaction is built. The example shows that the loan a borrower experiences as a single event is in fact the coordinated work of many specialized parties, each introduced somewhere in this book.

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