

REAL ESTATE PRINCIPLES — AND — PRACTICES

Fifth Edition



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PREFACE

GOALS OF THIS TEXTBOOK

This book is designed to provide a thorough understanding of the nature and practice of real estate from the practical viewpoint. It deals with a broad span of topics, and provides an in-depth coverage of appropriate subjects. This broad coverage gives the reader the background needed in everyday life and in various careers, and at the same time provides a basis for more specialized courses required for a real estate professional position. The book that also deals with contemporary and emerging issues related to real estate may affect a person purchasing or selling a home or considering real estate as an investment.

RATIONALE

This text assumes that the student has no prior educational or business background in real estate, and the topics are written accordingly. We have presented the concepts and practices in an understandable fashion, while retaining an appropriate depth of coverage needed by real estate professionals. Initially we introduce the basic principles and concepts of real estate, and then we explain their application to real estate practices. This text and its supplementary materials are intended for use in any of the following:

1. Basic courses in real estate at the university or community college level
2. Introductory college level courses to prepare students for more specialized courses such as real estate finance, investments, law and appraisal
3. Adult education courses designed primarily for investors, homeowners, and others seeking an understanding of the principles and practices of real estate
4. Courses directed primarily toward persons preparing for state real estate licensing examinations
5. As a reference for persons seeking to increase their professional skills as practicing brokers or salespersons, loan officers, mortgage bankers, trust officers, or farm managers

TEXT ORGANIZATION

The chapters in the text were sequenced to provide steps in a learning process so that chapters build upon one another. The first five chapters provide basic legal information the student needs for later topics. Chapters 6 through 12 proceed into the practical topics of real estate practices, including leasing and financing. Chapters 13 through 15 cover brokerage, marketing, and licensing. Chapters 16 and 17 summarize the closing of a residential transaction. The instructor can choose from the remaining chapters, placing preferred degrees of emphasis on these topics, possibly omitting chapters or portions of chapters.

NEW TO THIS EDITION

Real estate is a dynamic and exciting field. The changes in practice, legislation, and theory require constant attention. In this fifth edition, we have thoroughly revised every chapter. Some of the more important changes and new coverage include:

1. Updates in the finance chapters to cover current HUD rules and current practices in the secondary market. This includes coverage of the new FAMC (Farmer Mac).
2. New government assistance corporations established to help bail out FCS and FSLIC and other developments in the Savings and Loan industry.
3. New types of mortgages such as price level adjusted mortgage (PLAM), as well as REMTS and REMICS.
4. Recent developments related to buyer brokerage and new state requirements for disclosures by agents to potential buyers, as well as degrees of protection given to agents through errors and omissions insurance.
5. New developments related to home inspection, radon inspection, and steel fabrication in single family residential construction, along with changes in the 1974 manufactured housing act.
6. Risks placed on buyers by new environmental lien laws.
7. New cases related to downzoning and laws prohibiting spot zoning. Other recent court cases are cited where they affect rights of buyers, sellers, agents, property owners, and the public.
8. Revisions to Chapters 11 and 21, reflecting the impact of tax law changes on home ownership and investments.
9. New problems causing increased FHA foreclosures. HUD's trial plan to support reverse mortgages.
10. New rules to help alleviate abuses in property tax and insurance escrow accounts.
11. Fair Housing Amendment Act of 1988.

TEACHING PACKAGE

We have developed comprehensive supplementary materials to facilitate the learning process.

- The Instructor's Manual contains in-depth answers to the end-of-chapter problems in the text, and provides numerous multiple choice questions and selected case problems (with answers) for use by the instructor in preparing examinations.
- A computerized test bank is available to facilitate accurate preparation of examinations, giving the instructor a choice of questions.
- A set of over 150 updated transparency masters is also available to adopters.

QUALITY FIRST

This edition of *Real Estate Principles and Practices* was prepared under the Merrill Quality First concept. As professors, we are assured by this program that the publisher has expended extra effort, time, and resources to assure that Merrill books uniquely meet the needs of students and faculty.

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CHAPTER 1

The Real Estate Business

OUTLINE

WHY WE STUDY REAL ESTATE

PROPERTY RESOURCES

REAL ESTATE OCCUPATIONS AND CAREERS

CHARACTERISTICS OF REAL ESTATE

THE REAL ESTATE MARKET

Real estate includes land and the structures built upon the land. We encounter real estate every day in our home living, our occupations, and our outside activities, and it makes up a substantial portion of the wealth of this or any nation. Land is a valuable asset that we must learn to conserve and to utilize effectively.

WHY WE STUDY REAL ESTATE

Each one of us owns or rents real estate to meet our basic housing needs, and the money we pay for housing represents a significant portion of our personal income. If we purchase a home, we are making a significant investment. Therefore, when we make a decision to rent or buy, or when we select between buying alternatives, we are making an important life decision. Although we might first think of real estate as a possible career when we begin to study this subject, knowledge of real estate is also very helpful in our personal lives. Real estate ownership has been a sound investment over the past fifty years. An understanding of real property, what gives it value, and the risks involved are important to each of us.

By recent estimates, the value of taxable real estate in the United States is especially impressive when we compare it to the value of stocks on the three major stock exchanges and to the value of savings and currency in circulation (see Figure 1-1).

The differences become more significant when we realize what a large amount of nontaxable real estate—not included in these figures—is owned by the federal and state governments and by tax-exempt organizations. These figures tend to highlight the importance of real estate in our economy.

A study of real estate also provides an opportunity to consider the many real estate career opportunities. These careers provide rewarding and interesting fields of work. In addition to the careers directly involving real estate sales and brokerage, every business is actually involved with real estate. Each business needs an office or building in which to operate. The selection of location and type of structure on the site can have a serious impact on the success of the business. Real estate also provides opportunities for investment, either personally or from a business standpoint. Knowledge of real estate will help us in evaluating investment opportunities. Thus, we see that the study of real estate provides an opportunity to evaluate a variety of career possibilities and gives us knowledge useful in our personal or business affairs.

PROPERTY RESOURCES

Before proceeding into the legal, economic, and business aspects of real estate, we will discuss several types of properties. Raw land has a wide variety of uses—food production; recreation; development into residential housing, factories, or commercial establishments. Land containing structures is called *improved property* and can be classified as residential, farm, commercial, industrial, or recreational. These cat-

Figure 1-1 Importance of real estate—shown by comparison

