FIN-331 PHASE 2 HOMEWORK QUESTIONS

Chapter 7: Define or describe the following Key Terms
Accrued depreciation
Appraisal
Comparable properties
Market value
Property adjustments
Replacement cost
Reproduction cost
Restricted appraisal report
Transactional adjustments

Chapter 7: Study Questions
2. What main difficulty would you foresee in attempting to estimate the value of a 30-year old property by means of the cost approach?

3. The cost approach to market valuation does not work well in markets that are overbuilt. Explain.

4. What is meant by functional obsolescence? Could a new building suffer from functional obsolescence?

7. What is a self-contained appraisal report?

8. What is the difference between market value and investment value?

12. In the sales comparison approach, if the comparable property is superior to the subject property in some way, is an upward or downward adjustment to the sale price of the comparable required? Explain.
Chapter 8: Define or describe the following Key Terms

Capital Expenditures
Direct capitalization
Effective gross income
Effective gross income multiplier
Capitalization rate
Natural vacancy rate
Net operating income
Operating expenses

Chapter 8: Study Questions

1. Data for five comparable income properties that sold recently are shown below:

<table>
<thead>
<tr>
<th>Property</th>
<th>NOI</th>
<th>Sale Price</th>
<th>Overall Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>$57,800</td>
<td>$566,600</td>
<td>0.1020</td>
</tr>
<tr>
<td>B</td>
<td>49,200</td>
<td>496,900</td>
<td>0.0990</td>
</tr>
<tr>
<td>C</td>
<td>63,000</td>
<td>630,000</td>
<td>0.1000</td>
</tr>
<tr>
<td>D</td>
<td>56,000</td>
<td>538,500</td>
<td>0.1040</td>
</tr>
<tr>
<td>E</td>
<td>58,500</td>
<td>600,000</td>
<td>0.0975</td>
</tr>
</tbody>
</table>

What is the indicated overall rate (RO)?

1. Use the following property data:

Cash flow from operations:

<table>
<thead>
<tr>
<th>Year</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>NOI</td>
<td>$150,000</td>
<td>$150,000</td>
<td>$150,000</td>
<td>$150,000</td>
<td>$150,000</td>
</tr>
<tr>
<td>Debt Service</td>
<td>$125,000</td>
<td>$125,000</td>
<td>$125,000</td>
<td>$125,000</td>
<td>$125,000</td>
</tr>
</tbody>
</table>

Cash Flow at sale:
Sale Price: $2,000,000  
Cost of sale: $125,000  
Mortgage balance: $1,500,000  
a. Assuming the going-in capitalization rate is 8.00%, compute a value for the property using direct capitalization.

Chapter 8: Study Questions (Continued)

5. Given the following owner's income and expense estimates for an apartment property, formulate a reconstructed operating statement. The building consists of 10 units that could rent for $550 per month each.

<table>
<thead>
<tr>
<th>Owner's Annual Income Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rental income (last year)</td>
</tr>
<tr>
<td>Less: Operating &amp; capital expenses</td>
</tr>
<tr>
<td>Power</td>
</tr>
<tr>
<td>Heat</td>
</tr>
<tr>
<td>Janitor</td>
</tr>
<tr>
<td>Water</td>
</tr>
<tr>
<td>Maintenance</td>
</tr>
<tr>
<td>Reserve for capital expenditures</td>
</tr>
<tr>
<td>Management</td>
</tr>
<tr>
<td>Tax depreciation</td>
</tr>
<tr>
<td>Mortgage payments</td>
</tr>
</tbody>
</table>

Estimating vacancy and collection losses at 5 percent of potential gross income, reconstruct the operating statement to obtain an estimate of NOI. Assume an above-line treatment of CAPX. Remember, there may be items in the owner's statement that should not be included in the reconstructed operating statement. Using the NOI and a Ro of 11.0%, calculate the property's indicated market value. Round your answer to the nearest $1,000.

6. You have been asked to estimate the market value of an apartment complex that is producing annual net operating income of $44,500. Four highly similar and competitive apartment properties within two blocks of the subject property have sold in the past three months. All four offer essentially the same amenities and services as the subject. All were open-market transactions with similar terms of sale. All were financed with 30-year fixed-rate
mortgages using 70 percent debt and 30 percent equity. The sale prices and estimated first-year net operating incomes were as follows:

Comparable 1:  Sale price $500,000; NOI $55,000
Comparable 2:  Sale price $420,000; NOI $50,400
Comparable 3:  Sale price $475,000; NOI $53,400
Comparable 4:  Sale price $600,000; NOI $69,000

What is the indicated value of the subject property using direct capitalization?

8. Describe the conditions under which the use of effective gross income multipliers to value the subject property is appropriate.
Chapter 9: Define or describe the following Key Terms

Adjustable-Rate Mortgage
Balloon Loan
Contract for Deed
Deed of Trust
Default Foreclosure
LIBOR
Negative Amortization
Nonrecourse Loans
Recourse Loans
Short Sale
Term to Maturity

Chapter 9: Study Questions

1. Mortgage law is as clear, consistent, and enforceable in the United States as in any place in the world, and far more so than in many countries. Why is this a vital element of an efficient real estate finance system?

4. Most lenders making adjustable rate mortgage loans offer a “teaser rate.” Is this a good policy or is it misrepresentation?

6. For your own state, determine whether:
   a. It is a judicial or non-judicial foreclosure state.
   b. The standard home loan is based on a deed of trust or a mortgage.
   c. There is a statutory right of redemption, and, if so, how long.
   d. Deficiency judgments are allowed against defaulted homeowners.

Based on this information can you judge your state is relatively debtor friendly or borrower friendly?
Chapter 10: Define or describe the following Key Terms

Alt-A Loan
Conforming Conventional Loan
Conventional Mortgage
Fannie Mae
Freddie Mac
FHA
GSE
Home Equity Loan
Jumbo Loans
Primary Mortgage Market
Secondary Mortgage Market
Reverse Mortgage
Subprime Loan

Chapter 10: Study Questions

1. On an adjustable mortgage, do borrowers always prefer smaller (i.e. tighter) rate caps that limit the amount the contract interest rate can increase in any given year or over the life if the loan? Explain why or why not.

2. Explain the potential tax advantages associated with home equity loans:

3. Distinguish between conforming and nonconforming residential mortgage loans and explain the importance of the difference.

4. Discuss the role and importance of private mortgage insurance in the residential mortgage market.

6. Suppose a homeowner has an existing mortgage loan with these terms: Remaining balance of $150,000, interest rate of 8%, and remaining term of 10 years (monthly payments). This loan can be replaced by a loan at an interest rate of 6 percent, at a cost of 8% of the outstanding loan amount. Should the homeowner refinance? What difference would it make if the homeowner expects to be in the home for only five more years?
Chapter 11: Define or describe the following Key Terms:

Collateral
Credit Scoring
Disintermediation
Housing Expense ratio
Interest rate Risk
Loan Underwriting
Pipeline Risk
Qualified Mortgage
Total Debt Ratio

Study Questions: 1, 2, 4, 9

1. What is the primary purpose of the risk-based capital requirements that Congress enacted as part of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA)?

2. Explain what is meant by forward commitments and standby forward commitments. Which part of the mortgage banker’s pipeline is often hedged with forward commitments? With standby forward commitments? Why?

4. Explain the importance of Fannie Mae and Freddie Mac to the housing finance system in the United States.

9. You have just signed a contract to purchase your dream house. The price is $120,000 and you have applied for a $100,000, 30-year, 5.5 percent loan. Annual property taxes are expected to be $2,000. Hazard insurance will cost $400 per year. Your car payment is $400, with 36 months left. Your monthly gross income is $5,000. Calculate:
   a. The monthly payment of principal and interest (PI).
   b. One-twelfth of annual property tax payments and hazard insurance payments.
   c. Monthly PITI (principal, interest, taxes, and insurance).
   d. The housing expense (front-end) ratio.
   e. The total obligations (back-end) ratio.
Chapter 12: Define or describe the following Key Terms

Fiduciary Relationship
Law of Agency
Open Listing
Principal vs. Agent

Chapter 13: Define or describe the following Key Terms

Assignment
Consideration
Earnest money
Equitable title
Escrow
Legal title
Rescission
Specific performance

Chapter 13: Question

1. How is the pro rata of miscellaneous charges accomplished? Example: insurance premiums, water and sewer charges, property taxes: review study questions one through four in text

   1. If a closing occurs on September 1 of a 365-day year, how will the year's property tax of $900 be prorated? (Note: the day of closing “belongs” to the buyer.)
   2. How would the hazard insurance premium be prorated?
   3. How would the water and sewer charges be prorated?
   4. How will the mortgage assumption be entered?