

**California Real Estate Finance**  
**Chapter 4**  
**Semifiduciary and Nonfiduciary Sources of Funds for Real Estate Finance**

**Chapter Purpose**

This chapter examines the lending activities of mortgage brokers, mortgage bankers and real estate investment and mortgage trusts. It also explores the use of bonds as a method to raise funds for real estate finance. In addition, the roles of endowment funds, title insurance companies, private loan companies and individuals who finance their own sales of property are examined to underscore the distinction between lenders who manage other peoples' monies and lenders who lend their own money.

**Suggestions to the Instructor**

The material in this chapter could be enhanced by the participation of a mortgage broker and/or a mortgage banker to describe their increasingly important roles in the real estate finance markets. A research assignment could also be made concerning the popularity (and necessity?) of the carry-back loan in your local market.

**Learning Objectives**

Upon completion of this chapter, the student should be able to:

1. compare and contrast the roles and responsibilities of the financial fiduciary, semifiduciary, and nonfiduciary lenders;
2. discuss the role of the mortgage broker in real estate finance;
3. understand the organization and scope of mortgage banking in providing local representation as correspondents for national mortgage investors;
4. understand the organization and activities of real estate investment and mortgage borrowers;
5. define the role of mortgage bonds in providing real estate finance for eligible borrowers;
6. realize the emerging importance of carry-back financing as a means for individuals selling their own property.

## **Presentation Outline**

- I. Semifiduciary Sources
  - A. Mortgage brokers
    1. Usually represent borrowers, charging them fees for services
    2. Prepare comprehensive loan applications
    3. Submit loan applications to various lenders seeking best deals for clients
    4. Do not lend their own money
    5. Do not service a loan once it is placed
    6. California real property loan law
      - a. controls fees that brokers can charge (see list in text)
      - b. specifies terms of junior finance loans
  - B. Mortgage bankers
    1. Mortgage bankers, also known as correspondents, represent their lenders
    2. They originate and service loans for a fee
    3. Development
      - a. began with lenders selling loans to investors while retaining loan service responsibilities
      - b. expanded as demand increased
      - c. exploded after FHA was created
    4. Operation
      - a. generally represents national lenders in specific local areas
      - b. derive income from loan origination and service fees
      - c. often create loans and then assign them to investors, keeping service contracts
      - d. highly competitive, taking active role in real estate community
  - C. Real estate trusts
    1. Investment conduits, avoids double income tax
      - a. must hold property mainly for investment
      - b. beneficial interests must be owned by at least 100 investors
      - c. no fewer than five persons may own more than 50% of the beneficial interests
      - d. must have transferable shares
      - e. 95% of income from its investments
      - f. 75% of income from real estate investments
      - g. 95% of income to be distributed annually
      - h. all trust income considered passive by IRS
    2. Real estate investment trusts (REITs)
      - a. invest in improved income properties
      - b. income derived from rents and capital gains
      - c. individual investor's personal liability limited to investment made
    3. Real estate mortgage trusts (REMTs)
      - a. invest mainly in real estate securities
      - b. income from origination fees, loan service contracts and interest
      - c. often invest in junior finance
      - d. sometimes become owner of real estate when foreclosure unavoidable

4. Combination real estate trusts (hybrid trusts)
  - a. combines both REIT and REMT
  - b. income from rents and loan payments
- D. California syndication (limited partnerships)
  1. Syndicates
    - a. organizations of investors pooling capital for real estate investments
    - b. can be corporations, general partnerships or limited partnerships
    - c. investment conduits that pass profits and losses through to investors in proportion to their ownership shares
    - d. controlled by the California Department of Corporations
  2. Limited partnerships
    - a. general partner responsible for managing partnership
    - b. limited partners do not participate in management
    - c. limited partners liability limited to their investment
    - d. limited partners may become liable for the total debts of the partnership if they take an active role in the management of the partnership
- E. Real estate bonds
  1. Nature of bonds
    - a. secured
    - b. unsecured (debentures)
    - c. coupon
    - d. registered coupon
    - e. mortgage, income, industrial or corporate
    - f. long-term, short-term or perpetual
    - g. convertible, redeemable, serial or sinking
    - h. refunding, construction, equipment or improvement
  2. Uses for bond issues
    - a. finance buildings
    - b. finance corporate capital expansion
    - c. finance corporate operations (debentures)
  3. Municipal and private bonds
    - a. general obligation bonds
    - b. revenue bonds
    - c. industrial revenue bonds
    - d. mortgage revenue bonds
    - e. zero coupon bonds
    - f. mortgage loan bonds

4. California bonds
    - a. mortgage revenue bonds
      - (1) issued by Community Redevelopment Agencies
      - (2) money used to make below-market interest rate loans to qualified developers of low-income and medium-income residential projects
    - b. mortgage-backed bonds
      - (1) issued by eligible savings associations
      - (2) to raise funds for real estate loans
      - (3) backed by pools of real estate loans
  - F. Endowment funds
    1. Provides a permanent source of income
    2. Managers responsible to develop income while preserving capital
    3. Perfect vehicle for real estate finance
- II. Nonfiduciary Sources of Funds
- A. Private loan companies
    1. Usually deal in junior finance
    2. Some encumber real property for additional collateral for financing personal property
    3. Often charge higher than market interest rates
    4. Must adhere to Truth-In-Lending laws
  - B. California Real Property Loan Law
  - C. Individual lenders
    1. Sellers as lenders
      - a. carry-backs to help sell property
      - b. usually junior loans
    2. Families as lenders
    3. Other lenders