

Contracts Lesson 8

- **Agency**
- The “agent” is the individual who is authorized and consents to represent the interests of the principal. The “principal” is the individual hiring the agent and granting to the agent the authority to represent the principal. A “fiduciary relationship” exists between the agent and the principal, meaning the agent is held in a position of special trust and confidence by the principal.
- There are three kinds of agents: (1) universal agent, (2) general agents, and (3) special agents. A “universal agent” has unlimited authority to perform any act on behalf of the principal. A “general agent” has far-reaching or wide authority to conduct a series of transactions of a continuous nature on behalf of the principal. For example, the vice-president of the western region of a company would be able to make all the decisions for the western region. A “special agent” has only limited authority to conduct a single transaction for the principal. A real estate broker and an attorney are examples of special agents. In real estate, a “single agent” means a broker who is engaged by and represents only one party in a transaction.
- **Right-to-Sell Agreements**
- The authority to act for a seller in a real estate transaction is given to the broker by means of a listing contract, which is simply an employment agreement between a property owner and the broker listing the property for sale. The listing may be either written or oral unless the broker is employed as an agent, in which case Colorado requires the agreement to be in writing. From a risk-reduction perspective, all listings should be in writing and signed by both owner and the broker in order to avoid misunderstandings that may arise later on. Commission Rule E-11 requires that all written listing contracts provide a definite date for termination.
- Colorado listing agreements provide that property sold within a holdover period after the listing term, to any party with whom the listing broker negotiated and whose name the broker submitted to the owner in writing, entitles the broker to a commission, even if the property is subsequently listed with another broker.

Contracts Lesson 8

- **Net Listing**
- A net listing is a contract to find a buyer or lessee for the property at a certain “net price to the owner.” For example: If an owner lists a property for \$100,000 net, and the broker finds a buyer at \$100,000 (or less), then the broker receives no commission. If the broker finds a buyer at \$115,000, the broker retains \$15,000 as earned commission. If the terms of a net listing agreement are challenged, courts may hold that the broker is not entitled to any amount exceeding the broker’s usual commission. Additionally, a broker who abuses a net listing may be found in violation, which deals with secret undisclosed profit. Because the Commission does not encourage net listings, there are no approved net-listing forms.
- **Open Listing**
- Under an open listing, the owner lists the property with a broker at a specified price, agreeing to pay a commission on that price or any offer acceptable to the owner. However, the owner retains the right to sell the property personally or to list the property with other brokers. This type of listing may be more common in small communities, where the seller is likely to be acquainted with all or most of the brokers and does not wish to antagonize the others by listing with only one. Only the broker who is the procuring cause of the sale is entitled to a commission. If the owner sells directly to a buyer without broker involvement, the owner is not obligated to pay compensation to any broker holding an open listing.
- **Exclusive Broker (Agency) Listing**
- Under an exclusive agency listing, the owner agrees that a commission will be payable only to the named broker, and that the property will not be listed with or sold by another broker. However, if the owner sells to a buyer procured without broker’s assistance, no commission is due. An exclusive agency listing, as compared to the net or open listing, permits the broker to apply his or her best efforts, unhampered by possible interference from other brokers, but still subject to the uncertainty of an owner sale.

Contracts Lesson 8

- **Exclusive Right-to-Sell Listing**
- This is similar to exclusive agency, except that the broker is given the sole and exclusive right to sell the property during the listing period. Even if the owner sells to a buyer procured by the owner, the broker is entitled to a commission. This type of listing is the most commonly used by brokers in Colorado. Brokers can apply their best efforts, secure in the knowledge that the right to a commission cannot be defeated by anyone during the listing period. The Commission-approved exclusive right-to-sell listing agreement is designed for use for both agency and transaction brokerage.
- **Multiple Listing**
- A multiple listing is not technically a separate listing or listing. It is, rather, a marketing arrangement. Broker-members of a local real estate association or multiple listing service (MLS) may combine to market their listings through the organization. Any member may then sell any property registered with the service and rely on a predetermined commission offered by the listing broker. The seller may choose whether to participate in MLS or an online property information exchange in the Commission-approved listing contracts. The seller also contracts in the listing as to which types of cooperating brokers will be offered how much compensation for bringing a buyer into the sale. Multiple listings are widely distributed and should never contain confidential seller information, such as the seller's motivation or willingness to accept a lower price or less favorable terms than those stated in the listing agreement.
- **Right-to-Buy Agreements**
- The authority to act for a buyer in the purchase of real estate is secured by means of an employment agreement between the broker and buyer. The agreement engages the broker to locate a property for the buyer at an acceptable price the terms. The information above concerning seller listings also applies to buyer listings or right-to-buy agreements, including the requirement for a definite termination date and the inclusion of a holdover period. The Commission-approved exclusive right-to-buy contract is designed for use for both agency and transaction-brokerage.

Contracts Lesson 8

- **Exclusive Right-to-Buy Contract**
- The broker agrees to assist (as a transaction-broker) or represent (as a agent) the purchaser or lessee by entering into a buyer listing agreement. The purchaser or lessee thus becomes the client/employer and compensates the broker for locating suitable property. With proper consent in the listing contract, the broker working with the buyer may seek compensation from the seller or the seller's broker. Brokers must make sure that clients fully understand the exclusive nature of this agreement. Clients who work with multiple brokers or directly with owners may create multiple contracts and commission obligations or precipitate litigation over breach of contract or procuring cause issues.
- **Closing Instructions**
- The Real Estate Commission, working in concert with the Division or Insurance, has developed a closing instructions form that must be used in conjunction with an approved listing contract. The closing instructions form provides for the appointment of a closing agent listing contract. The closing instructions form provides for the appointment of a closing agent and outlines responsibility for payment of fees for closing services. The Commission's position is that this form be initiated, with the buyer or seller, at the time a listing is signed. The form can then be completed with the signatures of both parties at the time of acceptance of a sales contract, and delivered to the closing entity in advance.
- **Sales Arrangements Between Brokers**
- Commission-approved seller listing contracts require the consent of the seller before a broker may offer commission splits to cooperating brokers.
- Together with the laws of agency and brokerage relationships, an understanding of contract law is essential for real estate practitioners. A licensee constantly reviews contracts for purchases, lease agreements, and mortgages. In Colorado, real estate licensees are allowed to fill in blanks in standard contract forms. The competency and professionalism of the real estate licensee are always at stake when contracts are being written or explained.

Contracts Lesson 8

- **Sales Arrangements Between Brokers cont.**
- Of all legal instruments, contracts are among the most important to our society and economic system. The stability and security of our business world are dependent upon the law of contracts. It ensures that parties perform their agreements by requiring that they either perform or pay for all loss or damage caused by non-performance. Furthermore, the specialized branches of business law, such as the sale of goods and services, negotiable instruments, partnerships and corporations, are all founded upon the law of contracts.
- A contract may be defined as an agreement between two or more competent persons, having for its purpose a legal object, wherein the parties agree to act in a certain manner.
- **Mutual Assent.**
- Before a valid contract exist, the parties must mutually consent to be bound by the terms of the agreement. Such mutual assent is evidenced or objectively set forth by the offer and acceptance. If the consent was obtained by fraud, misrepresentation, duress, undue influence, or mistake, then there is no real consent and, therefore, the element of mutual assent is absent. In certain cases, the law requires that the expression of the parties' mutual agreement be in writing to be enforceable.
- **Offer**
- An offer is a promise by one party to act in a certain manner provided the other party will act in the manner requested. The one making the offer is called the offeror; the one to whom the offer is made is called the offeree.
- **Acceptance**
- The second step in achieving mutual assent is the acceptance, the indication by the offeree that they are willing to be bound by the terms of the offer. In a real estate transaction, this is usually accomplished by the seller signing the offer to purchase made by the buyer.

Contracts Lesson 8

- **Reality of Consent**
- Fraud and misrepresentation are self-explanatory and, when present, permit the innocent party to cancel the contract and, in appropriate cases, to recover damages suffered.
- Undue influence consists of the abuse of the control or influence that one person has over another because of their relationship. Duress consists of compelling a person, through fear, to do or to agree to do an act.
- **Statute of Frauds**
- To prevent fraud through perjury, the law requires that the parties' agreement evidencing their mutual assent be in writing in certain cases. As to real estate in Colorado provides:
- Every contract for the leasing for a longer period than one year or for the sale of any lands or any interest in lands is void unless the contract or some note or memorandum thereof expressing the consideration is in writing and subscribed by the party by whom the lease or sale is to be made.
- **The Parol Evidence Rule**
- The parol evidence rule is closely linked to the statute of frauds. It provides that an agreement in writing shows that the parties intend it as the final and complete expression of their agreement. Evidence of any earlier oral or written statements is not admissible to vary, add to, or contradict the terms of the writing. The word parol means "word" or "speech." Because the purpose of the statute of frauds is to prevent the possibility of nonexistent agreements being enforced by fraud or perjury, it makes sense to have a rule that requires the parties to live with what they have written. The parol evidence rule generally keeps parties from trying to introduce evidence in court that they really meant something other than what is stated in the written contract.

Contracts Lesson 8

- **Consideration**
- Agreement alone does not make an enforceable contract. There must be consideration supporting the agreement. Many persons assume money is a requirement of consideration; but in the vast majority of cases the consideration for a promise is the return promise. The promise of the buyer to buy and the promise of the owner to sell constitute sufficient consideration to support their agreement - no deposit is necessary.
- Consideration may be defined as a promise or an act of legal value bargained for and received in return for a promise.
- **Competent Parties**
- All parties are presumed to have the legal capacity to enter into contracts. But certain persons, for reasons of public policy or some disability, do not have full contractual capacity. Among these are minors, mental defectives, and intoxicated persons.
- In Colorado, a minor is an individual under 18 years of age. Minors have the right to cancel or disaffirm their contracts with no liability other than the return of any proceeds they received under such contract. Minors are given this right to protect them against their lack of experience, judgment, and ability. The burden is upon adults to ascertain that the person they deal with is of legal age. After reaching legal age, minors may ratify or approve previous contracts, which will then be binding on them.
- Insane persons are given the same protection as that given to minors, except that the contracts of a person judicially declared insane could never have had effect in the first place.
- The contract of an intoxicated person is usually binding, except where that person is so intoxicated as to be incapable of understanding the nature of the transaction. In the case, the intoxicated person may cancel or ratify the contract.

Contracts Lesson 8

- **Legal Purpose**
- To be valid and enforceable, a contract must have a legal object for its purpose. The object cannot be to violate a valid statute. An agreement to commit a crime, a tort, or something contrary to public welfare is illegal. For example, an agreement to defraud someone, slander a person, or operate an unauthorized gambling operation is illegal. Dual contracting to induce a lender to make a loan on real estate without knowing the true terms of sale, such as the actual amount of down payment, is a criminal offense.
- **Matters to be Considered in Real Estate Contracts**
- The buy-sell contract is the most important document in a real estate transaction. This contract determines the kind of title to be conveyed, the type of deed, liens and encumbrances that the land will be sold subject to, and the manner of payment of the purchase price.
- Numerous controversies involving real estate licensees arise out of contracts for the sale of property. Although dishonesty or wrongdoing on the part of the licensee is rare, disputes often stem from the licensee's lack of thoroughness or knowledge. Real estate brokers must continually strive to increase their own proficiency and that of their employed licensees in writing good contracts. It is an art to write a sound, workable contract that includes all important matters and is still reasonably clear and understandable. Although Colorado licensees are fortunate in having Commission-approved contract forms available, they must nevertheless pay close attention to completing these forms in a competent manner.
- The following are the main items to be considered in drawing up real estate contracts. This list is not intended to be exhaustive; seldom are two real estate transactions alike. Only through careful study, experience, and guidance will the real estate licensee learn to recognize the essential items to be included in a given transaction.
- **Names and Signatures of the Parties**
- The seller and buyer must be named and properly designated as the seller (vendor) and buyer (vendee).

Contracts Lesson 8

- **Sale price and Payment Provisions**
- The contract is incomplete and unenforceable unless it contains the sales price. If there is no provision regarding the method of payment, the law presumes it is to be a cash sale.
- **Description of the Property**
- The description of the real estate should be sufficiently definite to identify the land sold with reasonable certainty. Although the street address, with the city and state, is sometimes sufficient, it is better to use the legal description contained in the seller's deed. Even though the contract may not mention them, additional rights to the land such as easements, rights of way and other appurtenances belonging to the land will automatically pass to the buyer in the transfer of ownership.
- **Type of Deed**
- The contract should provide for the type of deed by which the property will be conveyed, whether by quitclaim, general warranty, or other kind of deed. In the event the type of deed is not stated, the courts will probably require that kind of deed that is customary to that particular type of transaction in that locality.
- **Condition of Title**
- Real estate sales contracts traditionally provide that title is to be merchantable, that is, free from defects and which a reasonably prudent buyer is willing to accept. Even without this provision, the law presumes that merchantable title is to be conveyed. Mortgages, tax liens, and other liens and encumbrances are considered defects. Therefore, if the property is to be conveyed subject to a mortgage or other encumbrance or restriction, the contract should clearly state so.

Contracts Lesson 8

- **Default Provisions**
- The right of the parties should be stated in the event that one side fails to perform. The law, of course, gives the parties remedies for non-performance, but a lawsuit can be avoided if the parties mutually agree to a settlement beforehand. Therefore, provisions should be made as to the disposition of the buyer's deposit if the buyer defaults, and any other arrangements deemed appropriate.
- **Contingency Provisions**
- A buyer may be willing to buy, but may first have to accomplish something, such as borrow additional money or sell a presently owned property. An offer to purchase must clearly state such conditions. It is possible that the seller may also wish to provide for some contingency. Poorly written contingencies are one of the major causes of disputes between the parties and complaints against real estate licensees.
- **Possession**
- If the time of closing the transaction is different from the time that possession of the premises is to be given to the buyer, the date and time of possession should be stated.
- **Apportionment or Adjustment**
- The contract should provide for the apportionment of all charges or assets concerning the property, such as taxes, assessments, water rents, interest on assumed encumbrances, mortgage insurance premiums, or rents.
- **Risk of Loss**
- If the property is damaged or destroyed by fire, flood, or storm after the contract is signed but before the deed is delivered, who suffers the loss—the seller or the buyer? The answer is not as simple as it seems.
- In most jurisdictions, when a binding real estate contract exists, and where either party may enforce specific performance, the loss falls upon the buyer who is considered the owner of the property. The buyer can legally force the seller to convey the legal title. Also, the seller can force the buyer to accept the legal title and perform their part. This right is called specific performance; the parties lose this right only if they waive it in the contract.

Contracts Lesson 8

- **Risk of Loss cont.**
- Some courts interpret equitable title theory as unjustly putting the burden of loss on the buyer. Not being in possession, the buyer is unable to protect his or her interest. However, the majority of courts seem to hold that the loss falls on the buyer unless the contract provides otherwise. To avoid potential misunderstanding or controversy, it is important to clearly spell out risk in the contract. It is not unusual for the contract of sale to provide that the risk of loss remains with the seller.
- **Earnest Money**
- Earnest money deposits are another critical element of any contract. Earnest money should be adequate to demonstrate the buyer's serious intent to purchase and, in the event of the buyer's default, to compensate the seller for the act of taking the property off the market during the period prior to closing. Earnest money should apply only to partial payment of the purchase price. The form of earnest money, check or promissory note, must be specified in the contract. If it is a note, it must have a definite due date. The Commission strongly recommends that notes not be taken with due dates of "at closing." Such notes create confusion as to the seller's forfeiture rights if closing does not occur and the buyer is at fault.
- **Loan Contingency**
- The ordinary buyer can only buy if he or she is able to borrow sufficient funds on reasonable terms. Ethical procedure demands that the contract be made contingent upon the ability to secure such a loan. If a buyer is unable to buy unless the sale of his or her current home is consummated, any offer should reflect this contingency. Such a contingency is still needed even if there is a pending contract to sell the buyer's home, if the buyer requires the proceeds from the sale in order to purchase, because there is never complete certainty that a pending sale transaction will close.

Contracts Lesson 8

- **Assumptions**
- When an existing mortgage will remain on the property after sale, the responsibility of the parties must be carefully set forth. The buyer may “assume and agree to pay” the existing mortgage or may buy the property “subject to” the existing mortgage. A seller will usually want the buyer to “assume and agree to pay” because it will make the buyer responsible on the original note along with the seller. In either case, both parties to the transaction should be informed of the resultant effect of the sale. Too often, unscrupulous buyers of equities have purchased “subject to” or even agreed to “assume and pay” an existing loan. They then collect rents from the property for as long as possible, while deliberately defaulting on the loan payments and letting the property go into foreclosure. A resulting deficiency judgment would be against the original owner and seller rather than the buyer. Such conduct, known as “equity skimming,” is a criminal offense.
- **Buyer’s Creditworthiness**
- The licensee’s service to the seller is to procure a ready, willing, and able buyer. What is meant by “able”? Certainly it means more than the buyer’s ability to execute the contract and make the initial payment. The licensee has a duty to the seller to make a reasonable effort to determine if the buyer is truly able to buy the property. If the buyer is assuming an existing loan, or if the seller is carrying back a purchase money mortgage or conveying by means of an installment land contract, the seller is in a high-risk position. There is no third-party lending institution to determine the buyer’s qualifications. The typical residential seller is not a speculator, and does not wish to pursue foreclosure or to retake title to the sold property. The seller will likely depend upon the licensee for guidance. Although the licensee may have no legal obligations to investigate the buyer, the licensee at least has a duty to inform the seller of the inherent dangers in the transaction and to advise the seller to make some type of an investigation concerning the buyer’s ability or willingness to pay.

Contracts Lesson 8

- **Balloon Payments**
- If a buyer agrees to sign a second note and trust deed as part payment, the terms should be specifically set forth. If a note requires regular equal installments but will not be completely paid off at the time the note matures, a larger payment will be required at the maturity date. The buyer may be in danger of foreclosure if he or she is unable to raise the money for such a balloon payment. In such a case, the licensee should make the buyer and seller aware of this eventuality. At the time the balloon payment becomes due, the buyer may be dependent on the ability to refinance. Colorado law protects the borrower in this regard.
- **Surveys**
- Many properties have not been properly surveyed. This is true particularly in areas that have not been formally subdivided into platted parcels. Some subdivided areas also contain irregular lot sizes, and the survey may be questionable. Both the frontage in running feet and the acreage, which determines square footage, are important and both should be verified before quoting figures to a buyer. In some cases, improvements, such as fences or garages, encroach on boundary lines and only a survey will reveal the problem. A broker may be liable in such situations because brokers are assumed to have greater knowledge than that of buyer and sellers. The broker should recommend to both the buyer and seller that a survey be made.
- **Dual Contracting and Loan Fraud**
- Another matter covered by law involves presenting a false contract with a larger purchase price to the lender than the price shown on the contract under which the parties intend to consummate the transaction. This is called dual contracting to induce a loan and is prohibited by the Colorado Criminal Code.
- False or inflated down payments, failure to identify seller-assisted down payments or concessions, second trust deeds, “gift letters,” or any other matter not fully and accurately reflected in a buy-sell contract and resulting settlement statement may result in severe disciplinary and sometimes even criminal action against a licensee.

Contracts Lesson 8

- **Installment Contracts**
- “There is a significant potential for harm to the seller, buyer or assignee if the installment land contract is not properly drafted. Real estate brokers are prohibited from drafting a contract document that would reflect the terms of such a transaction as it would exceed their level of competency and is a matter requiring the expertise and advice of an attorney. Additionally, such behavior may be construed as the unauthorized practice of law by the real estate broker and subject to civil penalties. The contracts for these transactions should not be prepared by a real estate broker; rather, the documents should be drafted by a licensed Colorado attorney-at-law engaged for each particular transaction.”
- **Foreclosure**
- Foreclosure through public sale gave rise to a new concept of the mortgage not as a conveyance of the land, but only as a lien upon the property. Thus, the lien would be enforced through a public sale rather than giving the lender title to the property. If the land sold for more than the debt, the mortgagee would be paid in full and the balance would be awarded to the borrower. It logically followed that if the property sold for less than the debt, then any other assets of the mortgagor would be available to the mortgagee through a deficiency judgment and by virtue of the borrower having signed a note or bond that was secured by the mortgage.
- Under modern mortgage law in the United States, there are three theories as to the nature of mortgages: (1) lien, (2) title, and (3) intermediate theories.
- **Longer Cure Period**
- Under the old and new laws, the foreclosure process is essentially commenced by the filing of a “Notice of Election and Demand” with the Public Trustee. The Public Trustee then has ten working days in which to record the Notice of Election and Demand at the Clerk & Recorder’s office.

Contracts Lesson 8

- **No Owner's Right to Redeem**
- Under the new foreclosure law, if the property is non-agricultural, the Public Trustee must set up the foreclosure sale in the 110-125 day window after the recording of the Notice of Election and Demand. If the property is agricultural, the foreclosure sale must be set up in the 215-230 day window after the recording of the Notice of Election and Demand. Under the new law the borrower still has until noon the day before the foreclosure sale to cure monetary defaults.
- Under the new law, junior lien holders still have redemption rights. However, because there is no owner's redemption period, junior lien holders must now file their notices of intent to redeem within the 8 business day window after the foreclosure sale. The junior lien holders still have similar sequential redemption rights. (5 days)
- **Definitions**
- "Agricultural property" means property, none of which, on the date of recording of the deed of trust or other lien or at the time of the recording of the notice of election and demand or lis pendens, is:
 - a. Platted as a subdivision
 - b. Located within an incorporated town or city and county
 - c. Valued and assessed as other than agricultural property
- "Confirmation deed" means assent to the estate already created. By the confirmation, the parties further strengthen and give legal validity to the estate. A person may confirm and assent documents of conveyance executed by another person.
- "Cure statement" The use of good faith estimates is authorized, so long as the cure statement states that it is a good faith estimate effective through the last day to cure as indicated on the cure statement. The foreclosing party will file a statement of the cure amount with the public trustee.

Contracts Lesson 8

- **Definitions cont.**
- “Deed of trust” means a writing that evidences a promise to pay or a right to the payment of a monetary obligation, such as a promissory note, bond, negotiable instrument, a loan, credit, or similar agreement, or a monetary judgment entered by a court of competent jurisdiction.
- “Evidence of debt” means a writing that evidences a promise to pay or a right to the payment of a monetary obligation, such as a promissory note, bond, negotiable instrument, a loan, credit, or similar agreement, or a monetary judgment entered by a court of competent jurisdiction.
- “Junior lien” means a deed of trust or other lien or encumbrance upon the property for which the amount due and owing thereunder is subordinate to the deed of trust or other lien being foreclosed.
- “Lienor” including without limitation the holder of a certificate of purchase or certificate of redemption for property, issued upon the foreclosure of a deed of trust or other lien on the property.
- “Notice of election and demand” means a notice of election and demand for sale related to a public trustee foreclosure under this article.
- “Officer” means the public trustee or sheriff conducting a foreclosure under this article.
- **Recording notice of election and demand - record of sale**
- No later than ten business days following the receipt of the notice of election and demand, the public trustee shall review the documents filed and, if the filing is complete, cause the notice to be recorded in the office of the county clerk and recorder of the county where the property described in the notice is located.
- **Recording notice of election and demand - record of sale cont.**
- The public trustee shall retain in the public trustee’s records a printed or electronic copy of the notice of election and demand and the combined notice, as published. Such records shall be available for inspection by the public at the public trustee’s offices during the public trustee’s normal business hours.

Contracts Lesson 8

- **Usual Elements of a Deed of Trust or Mortgage**
- **Date.** Though not essential, inclusion of the date might prevent later controversy as to when the security interest was conveyed.
- **Parties.** All parties to mortgage or trust deed must be named and clearly designated. In a mortgage, they are the mortgagor (grantor) and mortgagee (grantee). In a deed of trust, they are the trustor (grantor), public trustee and beneficiary. The name of the grantor must be exactly the same as on the deed by which the grantor acquired title.
- **Consideration.** Consideration is the money loaned to the trustor or mortgagor, usually to assist in purchasing the property. The statement regarding the consideration should contain the following:
 - a. Description of the indebtedness
 - b. Amount
 - c. Maturity date
 - d. Method of repayment of the principal amount
 - e. Interest rate and time of payment
 - f. Interest coupon notes, if any
 - g. Conditions of default as to principal and interest
- **Words of Conveyance.** The words of conveyance should be “done hereby convey to” or something similar. This gives the trustee or mortgagee an interest in the property that will serve as security.
- **Legal Description.** This is necessary to identify the real estate subject to the security interest. This description should read the same as that contained in the deed by which title is transferred.
- **Usual Elements of a Deed of Trust or Mortgage cont.**
- **Method of sale in case of default.** The beneficiary of a trust deed may foreclose by public sale through the office of the public trustee or through the courts. In Colorado, the mortgagee or beneficiary of a private trust deed may foreclose only through the courts.
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Contracts Lesson 8

- **Exceptions as to prior liens, if any.**
- **Signature of the trustor/mortgagor.**
- **Acknowledgment.** Signing before a notary is the simplest means of establishing the instrument's proper execution and validity.
- **Recording.** Recording in the office of the county clerk and recorder of the county in which the property is situated is necessary to protect the interest of the beneficiary or mortgagee against the claim of persons who may thereafter acquire an interest in the property without actual notice of the mortgage or trust deed.
- **Assumption of Indebtedness**
- A buyer and seller may wish to transfer title with the existing loan remaining as a lien upon the property. This is accomplished by a provision in the contract whereby the buyer assumes and agrees to pay the existing indebtedness.
- However, assumption is subject to limitations that may be present in the mortgage or trust deed contract. Mortgages and trust deeds often contain a provision to the effect that if the subject property is conveyed, the entire balance of the loan becomes due. This has the same effect as an acceleration clause in the event of default.
- The above restriction may alternatively preclude conveyance without the lender's consent. This enables the lender to adjust the interest rate or other terms of the loan. If conveyance is made without the lender's consent, the lender may call the entire balance of the loan due.
- **The Promissory Note**
- In the real estate financing process, the principal promissory note or bond is the evidence of the debt for which the mortgage or deed of trust is the security. This note is an unconditional promise in writing, signed by the maker, agreeing to pay on demand or at some future time, a certain sum of money to the payee or bearer. A promissory note creates a personal liability on the part of the maker. In the event of a default, if the security is insufficient to cover the indebtedness, the holder of the note may obtain a deficiency judgment for the balance due and proceed against all other property and assets of the debtor.

Contracts Lesson 8

- **Second Mortgage or Trust Deed**
- When the first deed of trust is satisfied, subsequent encumbrances move upward in priority. The second trust deed would then become first in priority, the third becomes second, and so on. However, the priority of instruments may be controlled by their terms. For instance, the terms of a second deed of trust may allow its lien to continue to be subordinate to the existing first, or any substitution thereof, thus allowing the owner to replace the first deed of trust with another without disturbing the position of the lien holders below the first. This advantage is often very important to the grantor in matters pertaining to refinancing property.