

Chapter 5

Real Estate Finance Instruments

In This Chapter

Whether you work for a bank, a mortgage company, a mortgage broker, or other type of primary lender, or for an agency that is active in the secondary market, you must know some of the various forms, reports, and other documents you will encounter in your work. The “instruments” discussed in this chapter focus on the more common legal documents you will encounter as part of real estate transactions that are used to establish the rights and duties of the parties involved. These include legal instruments, such as promissory notes, security instruments, trust deeds, and mortgages. We’ll also discuss types and features of mortgages, as well as typical clauses found in these instruments.

At the end of this chapter, you will be able to:

- Contrast a financing instrument from a security instrument.
- Discuss advantages and disadvantages of trust deeds.
- Discuss advantages and disadvantages of mortgages.
- Define the purpose of different types of mortgages.
- Identify typical mortgage clauses.

Acceleration Clause
Alienation Clause
Balloon Payment
Construction Loan
Equitable Right of Redemption
Equitable Title
Hypothecate
Judicial Foreclosure
Mortgage
Negotiable Instrument
Non-Judicial Foreclosure
Note Rate
Promissory Note
Security Instrument
Subordination Agreement
Trust Deed (or Deed of Trust)

Promissory Notes

Promissory notes are *financing instruments that evidence a promise to pay a specific amount of money to a specific person within a specific time frame*. Simply stated, a promissory note is a written promise to pay money. Before a lender will finance the purchase of a house, the borrower must promise to repay the funds. The *one promising to pay the money* is called the **maker** of the note, usually the borrower. The *one to whom payment is promised* is called the **payee**, usually the lender, which could also be the seller. Promissory notes are basic evidence of debt, showing who owes how much to whom. A typical promissory note includes:

- Date
- Names of the parties
- Amount of the debt, including the interest rate used to amortize the debt, known as the **note rate**
- How and when the money is to be paid
- What happens in the event of default
- Signature of the maker

Most promissory notes used in real estate are **negotiable instruments**, which means that they are *freely transferable from one party to another*. When a note is freely transferable, the lender or other creditor can obtain immediate cash by selling the note, for example, when a lender sells real estate notes to the secondary market.

Types of Notes

The four types of notes usually used in real estate transactions are:

- **Straight Note or Interest Only Note.** Calls for payments of interest-only during the term of the note, with a balloon payment at the end of the loan term to pay off the principal amount; usually a short-term loan.
- **Installment Note.** Calls for payments of principal and/or interest at designated intervals, (in reality, a balloon payment may be required).
- **Partially Amortizing Installment Note or Installment Note with Balloon.** Calls for periodic payments of principal and interest during the loan term with a balloon payment at the end of the term to pay off the balance due.
- **Fully Amortizing Installment Note.** Calls for regular payment of principal and interest, calculated to pay off the entire balance by the end of loan term.

Security Instruments

In almost all real estate financing transactions, a promissory note is accompanied by a **security instrument**. A security instrument requires a debtor to **hypothecate** his or her property as a condition of a loan, which means that *a debtor pledges personal or real property as security for a debt, typically without giving up possession of it*.

A security instrument serves as protection for the creditor, and motivation for the debtor, to make sure that the terms of the note are fulfilled and the note is repaid as agreed. Keep in mind, though, that a security instrument just describes collateral for a note. Even without a security instrument, the debtor is still obligated to pay the note. Failure to repay the debt according to the terms of the agreement could result in foreclosure. When the debt is repaid, the note and the security instrument are cancelled.

The two main types of security instruments used in real estate transactions are trust deeds and mortgages.

NOTE

[Date]

[City]

[State]

[Property Address]

1. BORROWER'S PROMISE TO PAY

In return for a loan that I have received, I promise to pay U.S. \$_____ (this amount is called "Principal"), plus interest, to the order of the Lender. The Lender is _____.

I will make all payments under this Note in the form of cash, check or money order.

I understand that the Lender may transfer this Note. The Lender or anyone who takes this Note by transfer and who is entitled to receive payments under this Note is called the "Note Holder."

2. INTEREST

Interest will be charged on unpaid principal until the full amount of Principal has been paid. I will pay interest at a yearly rate of _____%.

The interest rate required by this Section 2 is the rate I will pay both before and after any default described in Section 6(B) of this Note.

3. PAYMENTS**(A) Time and Place of Payments**

I will pay principal and interest by making a payment every month.

I will make my monthly payment on the _____ day of each month beginning on _____, _____. I will make these payments every month until I have paid all of the principal and interest and any other charges described below that I may owe under this Note. Each monthly payment will be applied as of its scheduled due date and will be applied to interest before Principal. If, on _____, 20____, I still owe amounts under this Note, I will pay those amounts in full on that date, which is called the "Maturity Date."

I will make my monthly payments at _____ or at a different place if required by the Note Holder.

(B) Amount of Monthly Payments

My monthly payment will be in the amount of U.S. \$_____.

4. BORROWER'S RIGHT TO PREPAY

I have the right to make payments of Principal at any time before they are due. A payment of Principal only is known as a "Prepayment." When I make a Prepayment, I will tell the Note Holder in writing that I am doing so. I may not designate a payment as a Prepayment if I have not made all the monthly payments due under the Note.

I may make a full Prepayment or partial Prepayments without paying a Prepayment charge. The Note Holder will use my Prepayments to reduce the amount of Principal that I owe under this Note. However, the Note Holder may apply my Prepayment to the accrued and unpaid interest on the Prepayment amount, before applying my Prepayment to reduce the Principal amount of the Note. If I make a partial Prepayment, there will be no changes in the due date or in the amount of my monthly payment unless the Note Holder agrees in writing to those changes.

5. LOAN CHARGES

If a law, which applies to this loan and which sets maximum loan charges, is finally interpreted so that the interest or other loan charges collected or to be collected in connection with this loan exceed the permitted limits, then: (a) any such loan charge shall be reduced by the amount necessary to reduce the charge to the permitted limit; and (b) any sums already collected from me which exceeded permitted limits will be refunded to me. The Note Holder may choose to make this refund by reducing the Principal I owe under this Note or by making a direct payment to me. If a refund reduces Principal, the reduction will be treated as a partial Prepayment.

6. BORROWER'S FAILURE TO PAY AS REQUIRED

(A) Late Charge for Overdue Payments

If the Note Holder has not received the full amount of any monthly payment by the end of _____ calendar days after the date it is due, I will pay a late charge to the Note Holder. The amount of the charge will be _____% of my overdue payment of principal and interest. I will pay this late charge promptly but only once on each late payment.

(B) Default

If I do not pay the full amount of each monthly payment on the date it is due, I will be in default.

(C) Notice of Default

If I am in default, the Note Holder may send me a written notice telling me that if I do not pay the overdue amount by a certain date, the Note Holder may require me to pay immediately the full amount of Principal which has not been paid and all the interest that I owe on that amount. That date must be at least 30 days after the date on which the notice is mailed to me or delivered by other means.

(D) No Waiver By Note Holder

Even if, at a time when I am in default, the Note Holder does not require me to pay immediately in full as described above, the Note Holder will still have the right to do so if I am in default at a later time.

(E) Payment of Note Holder's Costs and Expenses

If the Note Holder has required me to pay immediately in full as described above, the Note Holder will have the right to be paid back by me for all of its costs and expenses in enforcing this Note to the extent not prohibited by applicable law. Those expenses include, for example, reasonable attorneys' fees.

7. GIVING OF NOTICES

Unless applicable law requires a different method, any notice that must be given to me under this Note will be given by delivering it or by mailing it by first class mail to me at the Property Address above or at a different address if I give the Note Holder a notice of my different address.

Any notice that must be given to the Note Holder under this Note will be given by delivering it or by mailing it by first class mail to the Note Holder at the address stated in Section 3(A) above or at a different address if I am given a notice of that different address.

8. OBLIGATIONS OF PERSONS UNDER THIS NOTE

If more than one person signs this Note, each person is fully and personally obligated to keep all of the promises made in this Note, including the promise to pay the full amount owed. Any person who is a guarantor, surety or endorser of this Note is also obligated to do these things. Any person who takes over these obligations, including the obligations of a guarantor, surety or endorser of this Note, is also obligated to keep all of the promises made in this Note. The Note Holder may enforce its rights under this Note against each person individually or against all of us together. This means that any one of us may be required to pay all of the amounts owed under this Note.

9. WAIVERS

I and any other person who has obligations under this Note waive the rights of Presentment and Notice of Dishonor. "Presentment" means the right to require the Note Holder to demand payment of amounts due. "Notice of Dishonor" means the right to require the Note Holder to give notice to other persons that amounts due have not been paid.

10. UNIFORM SECURED NOTE

This Note is a uniform instrument with limited variations in some jurisdictions. In addition to the protections given to the Note Holder under this Note, a Mortgage, Deed of Trust, or Security Deed (the "Security Instrument"), dated the same date as this Note, protects the Note Holder from possible losses which might result if I do not keep the promises which I make in this Note. That Security Instrument describes how and under what conditions I may be required to make immediate payment in full of all amounts I owe under this Note. Some of those conditions are described as follows:

If all or any part of the Property or any Interest in the Property is sold or transferred (or if Borrower is not a natural person and a beneficial interest in Borrower is sold or transferred) without Lender's prior written consent, Lender may require immediate payment in full of all sums secured by this Security Instrument. However, this option shall not be exercised by Lender if such exercise is prohibited by Applicable Law.

If Lender exercises this option, Lender shall give Borrower notice of acceleration. The notice shall provide a period of not less than 30 days from the date the notice is given in accordance with Section 15 within which Borrower must pay all sums secured by this Security Instrument. If Borrower fails to pay these sums prior to the expiration of this period, Lender may invoke any remedies permitted by this Security Instrument without further notice or demand on Borrower.

WITNESS THE HAND(S) AND SEAL(S) OF THE UNDERSIGNED.

(Seal)
- Borrower

(Seal)
- Borrower

(Seal)
- Borrower

[Sign Original Only]

SAMPLE

Trust Deeds

Trust deeds, or deeds of trust, are instruments *placing a specific financial interest in the title to real property into the hands of a disinterested third party as security for the payment of a note*. With a trust deed, the borrower is called the **trustor**; the lender is the **beneficiary** who retains both the note and the deed of trust; and the **trustee** who holds legal title to the security property described in the deed of trust subject to the terms of the trust for the benefit of the lender. Who is eligible to be a trustee varies from state to state; it could be an attorney, for example, or a title company that provides trustee services. With a trust deed, the borrower has possession of and **equitable title** to the property. When the loan is paid, the note and the deed of trust are cancelled and both legal title and equitable title are then vested in the borrower.

Another distinguishing characteristic of trust deeds is that the trustee has the authority under the terms of the trust to commence a **non-judicial foreclosure action** when the lender has declared the loan to be in default. Such action would not be taken, however, until after the trustee has notified the borrower of the default and given the borrower the opportunity to cure.

Mortgages

A **mortgage** is the *conveyance of an interest in real property to a lender as security for the payment of a note*. A mortgage is a type of security instrument where the borrower (the mortgagor) conveys an interest property to the lender (the mortgagee) as collateral for the debt, creating a **voluntary lien** on the property. When a borrower defaults on a mortgage, the lender may commence a **judicial foreclosure action**.

LIEN THEORY AND TITLE THEORY

Some states follow what is called lien theory, while others follow what is called title theory.

Generally speaking, in **lien theory** states, the *security instrument creates a lien against the property which must be repaid by the debtor*. The property serves as collateral that is hypothecated to the lender as security for the debt, but the mortgagor holds the title to the property (or equitable title if a deed of trust is used). The lender may be required to go through a judicial foreclosure proceeding to obtain title and possession in the event of default.

In **title theory** states, the *security instrument gives actual title to the property to the lender while the debt is outstanding, with the borrower retaining only equitable title and possession of the land*. Once the mortgage amount has been repaid, legal title reverts or is conveyed to the borrower. The lender does not have possession or use of the property, and would have to go through a foreclosure proceeding to gain possession in the event of default, although it may be possible to avoid the lengthy judicial foreclosure proceeding and gain possession through non-judicial or strict foreclosure.

Some lien theory states allow only mortgages to be recorded; some title theory states allow only trust deeds to be recorded; and some states will allow either type of security instrument to be recorded. Make certain that you understand how mortgages and deeds of trust are handled in the states in which you practice.

After Recording Return To:

[Space Above This Line For Recording Data] _____

MORTGAGE

DEFINITIONS

Words used in multiple sections of this document are defined below and other words are defined in Sections 3, 11, 13, 18, 20 and 21. Certain rules regarding the usage of words used in this document are also provided in Section 16.

(A) **“Security Instrument”** means this document, which is dated _____, _____, together with all Riders to this document.

(B) **“Borrower”** is _____. Borrower is the mortgagor under this Security Instrument.

(C) **“Lender”** is _____. Lender is a _____ organized and existing under the laws of _____. Lender’s address is _____. Lender is the mortgagee under this Security Instrument.

(D) **“Note”** means the promissory note signed by Borrower and dated _____, _____. The Note states that Borrower owes Lender _____ Dollars (U.S. \$ _____) plus interest. Borrower has promised to pay this debt in regular Periodic Payments and to pay the debt in full not later than _____.

(E) **“Property”** means the property that is described below under the heading “Transfer of Rights in the Property.”

(F) **“Loan”** means the debt evidenced by the Note, plus interest, any prepayment charges and late charges due under the Note, and all sums due under this Security Instrument, plus interest.

(G) **“Riders”** means all Riders to this Security Instrument that are executed by Borrower. The following Riders are to be executed by Borrower [check box as applicable]:

- | | | |
|--|---|---|
| <input type="checkbox"/> Adjustable Rate Rider | <input type="checkbox"/> Condominium Rider | <input type="checkbox"/> Second Home Rider |
| <input type="checkbox"/> Balloon Rider | <input type="checkbox"/> Planned Unit Development Rider | <input type="checkbox"/> Other(s) [specify] _____ |
| <input type="checkbox"/> 1-4 Family Rider | <input type="checkbox"/> Biweekly Payment Rider | |

(H) **“Applicable Law”** means all controlling applicable federal, state and local statutes, regulations, ordinances and administrative rules and orders (that have the effect of law) as well as all applicable final, non-appealable judicial opinions.

(I) **“Community Association Dues, Fees, and Assessments”** means all dues, fees, assessments and other charges that are imposed on Borrower or the Property by a condominium association, homeowners association or similar organization.

(J) **“Electronic Funds Transfer”** means any transfer of funds, other than a transaction originated by check, draft, or similar paper instrument, which is initiated through an electronic terminal, telephonic instrument, computer, or magnetic tape so as to order, instruct, or authorize a financial institution to debit or credit an account. Such term includes, but is not limited to, point-of-sale transfers, automated teller machine transactions, transfers initiated by telephone, wire transfers, and automated clearinghouse transfers.

(K) “Escrow Items” means those items that are described in Section 3.

(L) “Miscellaneous Proceeds” means any compensation, settlement, award of damages, or proceeds paid by any third party (other than insurance proceeds paid under the coverages described in Section 5) for: (i) damage to, or destruction of, the Property; (ii) condemnation or other taking of all or any part of the Property; (iii) conveyance in lieu of condemnation; or (iv) misrepresentations of, or omissions as to, the value and/or condition of the Property.

(M) “Mortgage Insurance” means insurance protecting Lender against the nonpayment of, or default on, the Loan.

(N) “Periodic Payment” means the regularly scheduled amount due for (i) principal and interest under the Note, plus (ii) any amounts under Section 3 of this Security Instrument.

(O) “RESPA” means the Real Estate Settlement Procedures Act (12 U.S.C. §2601 et seq.) and its implementing regulation, Regulation X (24 C.F.R. Part 3500), as they might be amended from time to time, or any additional or successor legislation or regulation that governs the same subject matter. As used in this Security Instrument, “RESPA” refers to all requirements and restrictions that are imposed in regard to a “federally related mortgage loan” even if the Loan does not qualify as a “federally related mortgage loan” under RESPA.

(P) “Successor in Interest of Borrower” means any party that has taken title to the Property, whether or not that party has assumed Borrower’s obligations under the Note and/or this Security Instrument.

TRANSFER OF RIGHTS IN THE PROPERTY

This Security Instrument secures to Lender: (i) the repayment of the Loan, and all renewals, extensions and modifications of the Note; and (ii) the performance of Borrower’s covenants and agreements under this Security Instrument and the Note. For this purpose, Borrower does hereby

mortgage, grant and convey to Lender the following described property located in the _____ of _____:

[Type of Recording Jurisdiction]

[Name of Recording Jurisdiction]

which currently has the address of _____

[Street]

_____, Ohio _____ (“Property Address”):

[City]

[Zip Code]

TOGETHER WITH all the improvements now or hereafter erected on the property, and all easements, appurtenances, and fixtures now or hereafter a part of the property. All replacements and additions shall also be covered by this Security Instrument. All of the foregoing is referred to in this Security Instrument as the “Property.”

BORROWER COVENANTS that Borrower is lawfully seised of the estate hereby conveyed and has the right to mortgage, grant and convey the Property and that the Property is unencumbered, except for encumbrances of record. Borrower warrants and will defend generally the title to the Property against all claims and demands, subject to any encumbrances of record.

THIS SECURITY INSTRUMENT combines uniform covenants for national use and non-uniform covenants with limited variations by jurisdiction to constitute a uniform security instrument covering real property.

UNIFORM COVENANTS. Borrower and Lender covenant and agree as follows:

1. Payment of Principal, Interest, Escrow Items, Prepayment Charges, and Late Charges. Borrower shall pay when due the principal of, and interest on, the debt evidenced by the Note and any prepayment charges and late charges due under the Note. Borrower shall also pay funds for Escrow Items pursuant to Section 3. Payments due under the Note and this Security Instrument shall be made in U.S. currency. However, if any check or other instrument received by Lender as payment under the Note or this Security Instrument is returned to Lender unpaid, Lender may require that any or all subsequent payments due under the Note and this Security Instrument be made in one or more of the following forms, as selected by Lender: (a) cash; (b) money order; (c) certified check, bank check, treasurer's check or cashier's check, provided any such check is drawn upon an institution whose deposits are insured by a federal agency, instrumentality, or entity; or (d) Electronic Funds Transfer.

Payments are deemed received by Lender when received at the location designated in the Note or at such other location as may be designated by Lender in accordance with the notice provisions in Section 15. Lender may return any payment or partial payment if the payment or partial payments are insufficient to bring the Loan current. Lender may accept any payment or partial payment insufficient to bring the Loan current, without waiver of any rights hereunder or prejudice to its rights to refuse such payment or partial payments in the future, but Lender is not obligated to apply such payments at the time such payments are accepted. If each Periodic Payment is applied as of its scheduled due date, then Lender need not pay interest on unapplied funds. Lender may hold such unapplied funds until Borrower makes payment to bring the Loan current. If Borrower does not do so within a reasonable period of time, Lender shall either apply such funds or return them to Borrower. If not applied earlier, such funds will be applied to the outstanding principal balance under the Note immediately prior to foreclosure. No offset or claim which Borrower might have now or in the future against Lender shall relieve Borrower from making payments due under the Note and this Security Instrument or performing the covenants and agreements secured by this Security Instrument.

2. Application of Payments or Proceeds. Except as otherwise described in this Section 2, all payments accepted and applied by Lender shall be applied in the following order of priority: (a) interest due under the Note; (b) principal due under the Note; (c) amounts due under Section 3. Such payments shall be applied to each Periodic Payment in the order in which it became due. Any remaining amounts shall be applied first to late charges, second to any other amounts due under this Security Instrument, and then to reduce the principal balance of the Note.

If Lender receives a payment from Borrower for a delinquent Periodic Payment which includes a sufficient amount to pay any late charge due, the payment may be applied to the delinquent payment and the late charge. If more than one Periodic Payment is outstanding, Lender may apply any payment received from Borrower to the repayment of the Periodic Payments if, and to the extent that, each payment can be paid in full. To the extent that any excess exists after the payment is applied to the full payment of one or more Periodic Payments, such excess may be applied to any late charges due. Voluntary prepayments shall be applied first to any prepayment charges and then as described in the Note.

Any application of payments, insurance proceeds, or Miscellaneous Proceeds to principal due under the Note shall not extend or postpone the due date, or change the amount, of the Periodic Payments.

3. Funds for Escrow Items. Borrower shall pay to Lender on the day Periodic Payments are due under the Note, until the Note is paid in full, a sum (the "Funds") to provide for payment of amounts due for: (a) taxes and assessments and other items which can attain priority over this Security Instrument as a lien or encumbrance on the Property; (b) leasehold payments or ground rents on the Property, if any; (c) premiums for any and all insurance required by Lender under Section 5; and (d) Mortgage Insurance premiums, if any, or any sums payable by Borrower to Lender in lieu of the payment of Mortgage Insurance premiums in accordance with the provisions of Section 10. These items are called "Escrow Items." At origination or at any time during the term of the Loan, Lender may require that Community Association Dues, Fees, and Assessments, if any be escrowed by Borrower, and such dues, fees and assessments shall be an Escrow Item. Borrower shall promptly furnish to Lender all notices of amounts to be paid under this Section. Borrower shall pay Lender the Funds for Escrow Items unless Lender waives Borrower's obligation to pay the Funds for any or all Escrow Items. Lender may waive Borrower's obligation to pay to Lender Funds for any or all Escrow Items at any time. Any such waiver may only be in writing. In the event of such waiver, Borrower shall pay directly, when and where payable, the amounts due for any Escrow Items for which payment of Funds has been waived by Lender and, if Lender requires, shall furnish to Lender receipts evidencing such payment within such time period as Lender may require. Borrower's obligation to make such payments and to provide receipts shall for all purposes be deemed to be a covenant and agreement contained in this Security Instrument, as the phrase "covenant and agreement" is used in Section 9. If Borrower is obligated to pay Escrow Items directly, pursuant to a waiver, and Borrower fails to pay the amount due

for an Escrow Item, Lender may exercise its rights under Section 9 and pay such amount and Borrower shall then be obligated under Section 9 to repay to Lender any such amount. Lender may revoke the waiver as to any or all Escrow Items at any time by a notice given in accordance with Section 15 and, upon such revocation, Borrower shall pay to Lender all Funds, and in such amounts, that are then required under this Section 3.

Lender may, at any time, collect and hold Funds in an amount (a) sufficient to permit Lender to apply the Funds at the time specified under RESPA, and (b) not to exceed the maximum amount a lender can require under RESPA. Lender shall estimate the amount of Funds due on the basis of current data and reasonable estimates of expenditures of future Escrow Items or otherwise in accordance with Applicable Law.

The Funds shall be held in an institution whose deposits are insured by a federal agency, instrumentality, or entity (including Lender, if Lender is an institution whose deposits are so insured) or in any Federal Home Loan Bank. Lender shall apply the Funds to pay the Escrow Items no later than the time specified under RESPA. Lender shall not charge Borrower for holding and applying the Funds, annually analyzing the escrow account, or verifying the Escrow Items, unless Lender pays Borrower interest on the Funds and Applicable Law permits Lender to make such a charge. Unless an agreement is made in writing or Applicable Law requires interest to be paid on the Funds, Lender shall not be required to pay Borrower any interest or earnings on the Funds. Borrower and Lender can agree in writing, however, that interest shall be paid on the Funds. Lender shall give to Borrower, without charge, an annual accounting of the Funds as required by RESPA.

If there is a surplus of Funds held in escrow, as defined under RESPA, Lender shall account to Borrower for the excess funds in accordance with RESPA. If there is a shortage of Funds held in escrow, as defined under RESPA, Lender shall notify Borrower as required by RESPA, and Borrower shall pay to Lender the amount necessary to make up the shortage in accordance with RESPA, but in no more than 12 monthly payments. If there is a deficiency of Funds held in escrow, as defined under RESPA, Lender shall notify Borrower as required by RESPA, and Borrower shall pay to Lender the amount necessary to make up the deficiency in accordance with RESPA, but in no more than 12 monthly payments.

Upon payment in full of all sums secured by this Security Instrument, Lender shall promptly refund to Borrower any Funds held by Lender.

4. Charges; Liens. Borrower shall pay all taxes, assessments, charges, fines, and impositions attributable to the Property which can attain priority over this Security Instrument, leasehold payments or ground rents on the Property, if any, and Community Association Dues, Fees, and Assessments, if any. To the extent that these items are Escrow Items, Borrower shall pay them in the manner provided in Section 3.

Borrower shall promptly discharge any lien which has priority over this Security Instrument unless Borrower: (a) agrees in writing to the payment of the obligation secured by the lien in a manner acceptable to Lender, but only so long as Borrower is performing such agreement; (b) contests the lien in good faith by, or defends against enforcement of the lien in, legal proceedings which in Lender's opinion operate to prevent the enforcement of the lien while those proceedings are pending, but only until such proceedings are concluded; or (c) secures from the holder of the lien an agreement satisfactory to Lender subordinating the lien to this Security Instrument. If Lender determines that any part of the Property is subject to a lien which can attain priority over this Security Instrument, Lender may give Borrower a notice identifying the lien. Within 10 days of the date on which that notice is given, Borrower shall satisfy the lien or take one or more of the actions set forth above in this Section 4.

Lender may require Borrower to pay a one-time charge for a real estate tax verification and/or reporting service used by Lender in connection with this Loan.

5. Property Insurance. Borrower shall keep the improvements now existing or hereafter erected on the Property insured against loss by fire, hazards included within the term "extended coverage," and any other hazards including, but not limited to, earthquakes and floods, for which Lender requires insurance. This insurance shall be maintained in the amounts (including deductible levels) and for the periods that Lender requires. What Lender requires pursuant to the preceding sentences can change during the term of the Loan. The insurance carrier providing the insurance shall be chosen by Borrower subject to Lender's right to disapprove Borrower's choice, which right shall not be exercised unreasonably. Lender may require Borrower to pay, in connection with this Loan, either: (a) a one-time charge for flood zone determination, certification and tracking services; or (b) a one-time charge for flood zone determination and certification services and subsequent charges each time remappings or similar changes occur which reasonably might affect such determination or certification. Borrower shall also be responsible for the payment of any fees imposed by the Federal Emergency Management Agency in connection with the review of any flood zone determination resulting from an objection by Borrower.

If Borrower fails to maintain any of the coverages described above, Lender may obtain insurance coverage, at Lender's option and Borrower's expense. Lender is under no obligation to purchase any particular type or amount of coverage. Therefore, such coverage shall cover Lender, but might or might not protect Borrower, Borrower's equity in the Property, or the contents of the Property, against any risk, hazard or liability and might provide greater or lesser coverage than was previously in effect. Borrower acknowledges that the cost of the insurance coverage so obtained might significantly exceed the cost of insurance that Borrower could have obtained. Any amounts disbursed by Lender under this Section 5 shall become additional debt of Borrower secured by this Security Instrument. These amounts shall bear interest at the Note rate from the date of disbursement and shall be payable, with such interest, upon notice from Lender to Borrower requesting payment.

All insurance policies required by Lender and renewals of such policies shall be subject to Lender's right to disapprove such policies, shall include a standard mortgage clause, and shall name Lender as mortgagee and/or as an additional loss payee. Lender shall have the right to hold the policies and renewal certificates. If Lender requires, Borrower shall promptly give to Lender all receipts of paid premiums and renewal notices. If Borrower obtains any form of insurance coverage, not otherwise required by Lender, for damage to, or destruction of, the Property, such policy shall include a standard mortgage clause and shall name Lender as mortgagee and/or as an additional loss payee.

In the event of loss, Borrower shall give prompt notice to the insurance carrier and Lender. Lender may make proof of loss if not made promptly by Borrower. Unless Lender and Borrower otherwise agree in writing, any insurance proceeds, whether or not the underlying insurance was required by Lender, shall be applied to restoration or repair of the Property, if the restoration or repair is economically feasible and Lender's security is not lessened. During such repair and restoration period, Lender shall have the right to hold such insurance proceeds until Lender has had an opportunity to inspect such Property to ensure the work has been completed to Lender's satisfaction, provided that such inspection shall be undertaken promptly. Lender may disburse proceeds for the repairs and restoration in a single payment or in a series of progress payments as the work is completed. Unless an agreement is made in writing or Applicable Law requires interest to be paid on such insurance proceeds, Lender shall not be required to pay Borrower any interest or earnings on such proceeds. Fees for public adjusters, or other third parties, retained by Borrower shall not be paid out of the insurance proceeds and shall be the sole obligation of Borrower. If the restoration or repair is not economically feasible or Lender's security would be lessened, the insurance proceeds shall be applied to the sums secured by this Security Instrument, whether or not then due, with the excess, if any, paid to Borrower. Such insurance proceeds shall be applied in the order provided for in Section 2.

If Borrower abandons the Property, Lender may file, negotiate and settle any available insurance claim and related matters. If Borrower does not respond within 30 days to a notice from Lender that the insurance carrier has offered to settle a claim, then Lender may negotiate and settle the claim. The 30-day period will begin when the notice is given. In either event, or if Lender acquires the Property under Section 22 or otherwise, Borrower hereby assigns to Lender (a) Borrower's rights to any insurance proceeds in an amount not to exceed the amounts unpaid under the Note or this Security Instrument, and (b) any other of Borrower's rights (other than the right to any refund of unearned premiums paid by Borrower) under all insurance policies covering the Property, insofar as such rights are applicable to the coverage of the Property. Lender may use the insurance proceeds either to repair or restore the Property or to pay amounts unpaid under the Note or this Security Instrument, whether or not then due.

6. Occupancy. Borrower shall occupy, establish, and use the Property as Borrower's principal residence within 60 days after the execution of this Security Instrument and shall continue to occupy the Property as Borrower's principal residence for at least one year after the date of occupancy, unless Lender otherwise agrees in writing, which consent shall not be unreasonably withheld, or unless extenuating circumstances exist which are beyond Borrower's control.

7. Preservation, Maintenance and Protection of the Property; Inspections. Borrower shall not destroy, damage or impair the Property, allow the Property to deteriorate or commit waste on the Property. Whether or not Borrower is residing in the Property, Borrower shall maintain the Property in order to prevent the Property from deteriorating or decreasing in value due to its condition. Unless it is determined pursuant to Section 5 that repair or restoration is not economically feasible, Borrower shall promptly repair the Property if damaged to avoid further deterioration or damage. If insurance or condemnation proceeds are paid in connection with damage to, or the taking of, the Property, Borrower shall be responsible for repairing or restoring the Property only if Lender has released proceeds for such purposes. Lender may disburse proceeds for the repairs and restoration in a single payment or in a series of progress payments as the work is completed. If the insurance or condemnation proceeds are not sufficient

to repair or restore the Property, Borrower is not relieved of Borrower's obligation for the completion of such repair or restoration.

Lender or its agent may make reasonable entries upon and inspections of the Property. If it has reasonable cause, Lender may inspect the interior of the improvements on the Property. Lender shall give Borrower notice at the time of or prior to such an interior inspection specifying such reasonable cause.

8. Borrower's Loan Application. Borrower shall be in default if, during the Loan application process, Borrower or any persons or entities acting at the direction of Borrower or with Borrower's knowledge or consent gave materially false, misleading, or inaccurate information or statements to Lender (or failed to provide Lender with material information) in connection with the Loan. Material representations include, but are not limited to, representations concerning Borrower's occupancy of the Property as Borrower's principal residence.

9. Protection of Lender's Interest in the Property and Rights Under this Security Instrument. If (a) Borrower fails to perform the covenants and agreements contained in this Security Instrument, (b) there is a legal proceeding that might significantly affect Lender's interest in the Property and/or rights under this Security Instrument (such as a proceeding in bankruptcy, probate, for condemnation or forfeiture, for enforcement of a lien which may attain priority over this Security Instrument or to enforce laws or regulations), or (c) Borrower has abandoned the Property, then Lender may do and pay for whatever is reasonable or appropriate to protect Lender's interest in the Property and rights under this Security Instrument, including protecting and/or assessing the value of the Property, and securing and/or repairing the Property. Lender's actions can include, but are not limited to: (a) paying any sums secured by a lien which has priority over this Security Instrument; (b) appearing in court; and (c) paying reasonable attorneys' fees to protect its interest in the Property and/or rights under this Security Instrument, including its secured position in a bankruptcy proceeding. Securing the Property includes, but is not limited to, entering the Property to make repairs, change locks, replace or board up doors and windows, drain water from pipes, eliminate building or other code violations or dangerous conditions, and have utilities turned on or off. Although Lender may take action under this Section 9, Lender does not have to do so and is not under any duty or obligation to do so. It is agreed that Lender incurs no liability for not taking any or all actions authorized under this Section 9.

Any amounts disbursed by Lender under this Section 9 shall become additional debt of Borrower secured by this Security Instrument. These amounts shall bear interest at the Note rate from the date of disbursement and shall be payable, with such interest, upon notice from Lender to Borrower requesting payment.

If this Security Instrument is on a leasehold, Borrower shall comply with all the provisions of the lease. If Borrower acquires fee title to the Property, the leasehold and the fee title shall not merge unless Lender agrees to the merger in writing.

10. Mortgage Insurance. If Lender required Mortgage Insurance as a condition of making the Loan, Borrower shall pay the premiums required to maintain the Mortgage Insurance in effect. If, for any reason, the Mortgage Insurance coverage required by Lender ceases to be available from the mortgage insurer that previously provided such insurance and Borrower was required to make separately designated payments toward the premiums for Mortgage Insurance, Borrower shall pay the premiums required to obtain coverage substantially equivalent to the Mortgage Insurance previously in effect, at a cost substantially equivalent to the cost to Borrower of the Mortgage Insurance previously in effect, from an alternate mortgage insurer selected by Lender. If substantially equivalent Mortgage Insurance coverage is not available, Borrower shall continue to pay to Lender the amount of the separately designated payments that were due when the insurance coverage ceased to be in effect. Lender will accept, use and retain these payments as a non-refundable loss reserve in lieu of Mortgage Insurance. Such loss reserve shall be non-refundable, notwithstanding the fact that the Loan is ultimately paid in full, and Lender shall not be required to pay Borrower any interest or earnings on such loss reserve. Lender can no longer require loss reserve payments if Mortgage Insurance coverage (in the amount and for the period that Lender requires) provided by an insurer selected by Lender again becomes available, is obtained, and Lender requires separately designated payments toward the premiums for Mortgage Insurance. If Lender required Mortgage Insurance as a condition of making the Loan and Borrower was required to make separately designated payments toward the premiums for Mortgage Insurance, Borrower shall pay the premiums required to maintain Mortgage Insurance in effect, or to provide a non-refundable loss reserve, until Lender's requirement for Mortgage Insurance ends in accordance with any written agreement between Borrower and Lender providing for such termination or until termination is required by Applicable Law. Nothing in this Section 10 affects Borrower's obligation to pay interest at the rate provided in the Note.

Mortgage Insurance reimburses Lender (or any entity that purchases the Note) for certain losses it may incur if Borrower does not repay the Loan as agreed. Borrower is not a party to the Mortgage Insurance.

Mortgage insurers evaluate their total risk on all such insurance in force from time to time, and may enter into agreements with other parties that share or modify their risk, or reduce losses. These agreements are on terms and conditions that are satisfactory to the mortgage insurer and the other party (or parties) to these agreements. These agreements may require the mortgage insurer to make payments using any source of funds that the mortgage insurer may have available (which may include funds obtained from Mortgage Insurance premiums).

As a result of these agreements, Lender, any purchaser of the Note, another insurer, any reinsurer, any other entity, or any affiliate of any of the foregoing, may receive (directly or indirectly) amounts that derive from (or might be characterized as) a portion of Borrower's payments for Mortgage Insurance, in exchange for sharing or modifying the mortgage insurer's risk, or reducing losses. If such agreement provides that an affiliate of Lender takes a share of the insurer's risk in exchange for a share of the premiums paid to the insurer, the arrangement is often termed "captive reinsurance." Further:

(a) Any such agreements will not affect the amounts that Borrower has agreed to pay for Mortgage Insurance, or any other terms of the Loan. Such agreements will not increase the amount Borrower will owe for Mortgage Insurance, and they will not entitle Borrower to any refund.

(b) Any such agreements will not affect the rights Borrower has – if any – with respect to the Mortgage Insurance under the Homeowners Protection Act of 1998 or any other law. These rights may include the right to receive certain disclosures, to request and obtain cancellation of the Mortgage Insurance, to have the Mortgage Insurance terminated automatically, and/or to receive a refund of any Mortgage Insurance premiums that were unearned at the time of such cancellation or termination.

11. Assignment of Miscellaneous Proceeds; Forfeiture. All Miscellaneous Proceeds are hereby assigned to and shall be paid to Lender.

If the Property is damaged, such Miscellaneous Proceeds shall be applied to restoration or repair of the Property, if the restoration or repair is economically feasible and Lender's security is not lessened. During such repair and restoration period, Lender shall have the right to hold such Miscellaneous Proceeds until Lender has had an opportunity to inspect such Property to ensure the work has been completed to Lender's satisfaction, provided that such inspection shall be undertaken promptly. Lender may pay for the repairs and restoration in a single disbursement or in a series of progress payments as the work is completed. Unless an agreement is made in writing or Applicable Law requires interest to be paid on such Miscellaneous Proceeds, Lender shall not be required to pay Borrower any interest or earnings on such Miscellaneous Proceeds. If the restoration or repair is not economically feasible or Lender's security would be lessened, the Miscellaneous Proceeds shall be applied to the sums secured by this Security Instrument, whether or not then due, with the excess, if any, paid to Borrower. Such Miscellaneous Proceeds shall be applied in the order provided for in Section 2.

In the event of a total taking, destruction, or loss in value of the Property, the Miscellaneous Proceeds shall be applied to the sums secured by this Security Instrument, whether or not then due, with the excess, if any, paid to Borrower.

In the event of a partial taking, destruction, or loss in value of the Property in which the fair market value of the Property immediately before the partial taking, destruction, or loss in value is equal to or greater than the amount of the sums secured by this Security Instrument immediately before the partial taking, destruction, or loss in value, unless Borrower and Lender otherwise agree in writing, the sums secured by this Security Instrument shall be reduced by the amount of the Miscellaneous Proceeds multiplied by the following fraction: (a) the total amount of the sums secured immediately before the partial taking, destruction, or loss in value divided by (b) the fair market value of the Property immediately before the partial taking, destruction, or loss in value. Any balance shall be paid to Borrower.

In the event of a partial taking, destruction, or loss in value of the Property in which the fair market value of the Property immediately before the partial taking, destruction, or loss in value is less than the amount of the sums secured immediately before the partial taking, destruction, or loss in value, unless Borrower and Lender otherwise agree in writing, the Miscellaneous Proceeds shall be applied to the sums secured by this Security Instrument whether or not the sums are then due.

If the Property is abandoned by Borrower, or if, after notice by Lender to Borrower that the Opposing Party (as defined in the next sentence) offers to make an award to settle a claim for damages, Borrower fails to respond to Lender within 30 days after the date the notice is given, Lender is authorized to collect and apply the Miscellaneous Proceeds either to restoration or repair of the Property or to the sums secured by this Security Instrument, whether or not then due. "Opposing Party" means the third party that owes Borrower Miscellaneous Proceeds or the party against whom Borrower has a right of action in regard to Miscellaneous Proceeds.

Borrower shall be in default if any action or proceeding, whether civil or criminal, is begun that, in Lender's judgment, could result in forfeiture of the Property or other material impairment of Lender's interest in the Property or rights under this Security Instrument. Borrower can cure such a default and, if acceleration has occurred, reinstate as provided in Section 19, by causing the action or proceeding to be dismissed with a ruling that, in Lender's judgment, precludes forfeiture of the Property or other material impairment of Lender's interest in the Property or rights under this Security Instrument. The proceeds of any award or claim for damages that are attributable to the impairment of Lender's interest in the Property are hereby assigned and shall be paid to Lender.

All Miscellaneous Proceeds that are not applied to restoration or repair of the Property shall be applied in the order provided for in Section 2.

12. Borrower Not Released; Forbearance By Lender Not a Waiver. Extension of the time for payment or modification of amortization of the sums secured by this Security Instrument granted by Lender to Borrower or any Successor in Interest of Borrower shall not operate to release the liability of Borrower or any Successors in Interest of Borrower. Lender shall not be required to commence proceedings against any Successor in Interest of Borrower or to refuse to extend time for payment or otherwise modify amortization of the sums secured by this Security Instrument by reason of any demand made by the original Borrower or any Successors in Interest of Borrower. Any forbearance by Lender in exercising any right or remedy including, without limitation, Lender's acceptance of payments from third persons, entities or Successors in Interest of Borrower or in amounts less than the amount then due, shall not be a waiver of or preclude the exercise of any right or remedy.

13. Joint and Several Liability; Co-signers; Successors and Assigns Bound. Borrower covenants and agrees that Borrower's obligations and liability shall be joint and several. However, any Borrower who co-signs this Security Instrument but does not execute the Note (a "co-signer"): (a) is co-signing this Security Instrument only to mortgage, grant and convey the co-signer's interest in the Property under the terms of this Security Instrument; (b) is not personally obligated to pay the sums secured by this Security Instrument; and (c) agrees that Lender and any other Borrower can agree to extend, modify, forbear or make any accommodations with regard to the terms of this Security Instrument or the Note without the co-signer's consent.

Subject to the provisions of Section 18, any Successor in Interest of Borrower who assumes Borrower's obligations under this Security Instrument in writing, and is approved by Lender, shall obtain all of Borrower's rights and benefits under this Security Instrument. Borrower shall not be released from Borrower's obligations and liability under this Security Instrument unless Lender agrees to such release in writing. The covenants and agreements of this Security Instrument shall bind (except as provided in Section 20) and benefit the successors and assigns of Lender.

14. Loan Charges. Lender may charge Borrower fees for services performed in connection with Borrower's default, for the purpose of protecting Lender's interest in the Property and rights under this Security Instrument, including, but not limited to, attorneys' fees, property inspection and valuation fees. In regard to any other fees, the absence of express authority in this Security Instrument to charge a specific fee to Borrower shall not be construed as a prohibition on the charging of such fee. Lender may not charge fees that are expressly prohibited by this Security Instrument or by Applicable Law.

If the Loan is subject to a law which sets maximum loan charges, and that law is finally interpreted so that the interest or other loan charges collected or to be collected in connection with the Loan exceed the permitted limits, then: (a) any such loan charge shall be reduced by the amount necessary to reduce the charge to the permitted limit; and (b) any sums already collected from Borrower which exceeded permitted limits will be refunded to Borrower. Lender may choose to make this refund by reducing the principal owed under the Note or by making a direct payment to Borrower. If a refund reduces principal, the reduction will be treated as a partial prepayment without any prepayment charge (whether or not a prepayment charge is provided for under the Note). Borrower's acceptance of any such refund made by direct payment to Borrower will constitute a waiver of any right of action Borrower might have arising out of such overcharge.

15. Notices. All notices given by Borrower or Lender in connection with this Security Instrument must be in writing. Any notice to Borrower in connection with this Security Instrument shall be deemed to have been given to Borrower when mailed by first class mail or when actually delivered to Borrower's notice address if sent by other means. Notice to any one Borrower shall constitute notice to all Borrowers unless Applicable Law expressly requires otherwise. The notice address shall be the Property Address unless Borrower has designated a substitute notice address by notice to Lender. Borrower shall promptly notify Lender of Borrower's change of address. If Lender specifies a procedure for reporting Borrower's change of address, then Borrower shall only report a change of address through that specified procedure. There may be only one designated notice address under this Security Instrument at any one time. Any notice to Lender shall be given by delivering it or by mailing it by first class mail to Lender's address stated herein unless

Lender has designated another address by notice to Borrower. Any notice in connection with this Security Instrument shall not be deemed to have been given to Lender until actually received by Lender. If any notice required by this Security Instrument is also required under Applicable Law, the Applicable Law requirement will satisfy the corresponding requirement under this Security Instrument.

16. Governing Law; Severability; Rules of Construction. This Security Instrument shall be governed by federal law and the law of the jurisdiction in which the Property is located. All rights and obligations contained in this Security Instrument are subject to any requirements and limitations of Applicable Law. Applicable Law might explicitly or implicitly allow the parties to agree by contract or it might be silent, but such silence shall not be construed as a prohibition against agreement by contract. In the event that any provision or clause of this Security Instrument or the Note conflicts with Applicable Law, such conflict shall not affect other provisions of this Security Instrument or the Note which can be given effect without the conflicting provision.

As used in this Security Instrument: (a) words of the masculine gender shall mean and include corresponding neuter words or words of the feminine gender; (b) words in the singular shall mean and include the plural and vice versa; and (c) the word “may” gives sole discretion without any obligation to take any action.

17. Borrower’s Copy. Borrower shall be given one copy of the Note and of this Security Instrument.

18. Transfer of the Property or a Beneficial Interest in Borrower. As used in this Section 18, “Interest in the Property” means any legal or beneficial interest in the Property, including, but not limited to, those beneficial interests transferred in a bond for deed, contract for deed, installment sales contract or escrow agreement, the intent of which is the transfer of title by Borrower at a future date to a purchaser.

If all or any part of the Property or any Interest in the Property is sold or transferred (or if Borrower is not a natural person and a beneficial interest in Borrower is sold or transferred) without Lender’s prior written consent, Lender may require immediate payment in full of all sums secured by this Security Instrument. However, this option shall not be exercised by Lender if such exercise is prohibited by Applicable Law.

If Lender exercises this option, Lender shall give Borrower notice of acceleration. The notice shall provide a period of not less than 30 days from the date the notice is given in accordance with Section 15 within which Borrower must pay all sums secured by this Security Instrument. If Borrower fails to pay these sums prior to the expiration of this period, Lender may invoke any remedies permitted by this Security Instrument without further notice or demand on Borrower.

19. Borrower’s Right to Reinstate After Acceleration. If Borrower meets certain conditions, Borrower shall have the right to have enforcement of this Security Instrument discontinued at any time prior to the earliest of: (a) five days before sale of the Property pursuant to any power of sale contained in this Security Instrument; (b) such other period as Applicable Law might specify for the termination of Borrower’s right to reinstate; or (c) entry of a judgment enforcing this Security Instrument. Those conditions are that Borrower: (a) pays Lender all sums which then would be due under this Security Instrument and the Note as if no acceleration had occurred; (b) cures any default of any other covenants or agreements; (c) pays all expenses incurred in enforcing this Security Instrument, including, but not limited to, reasonable attorneys’ fees, property inspection and valuation fees, and other fees incurred for the purpose of protecting Lender’s interest in the Property and rights under this Security Instrument; and (d) takes such action as Lender may reasonably require to assure that Lender’s interest in the Property and rights under this Security Instrument, and Borrower’s obligation to pay the sums secured by this Security Instrument, shall continue unchanged. Lender may require that Borrower pay such reinstatement sums and expenses in one or more of the following forms, as selected by Lender: (a) cash; (b) money order; (c) certified check, bank check, treasurer’s check or cashier’s check, provided any such check is drawn upon an institution whose deposits are insured by a federal agency, instrumentality or entity; or (d) Electronic Funds Transfer. Upon reinstatement by Borrower, this Security Instrument and obligations secured hereby shall remain fully effective as if no acceleration had occurred. However, this right to reinstate shall not apply in the case of acceleration under Section 18.

20. Sale of Note; Change of Loan Servicer; Notice of Grievance. The Note or a partial interest in the Note (together with this Security Instrument) can be sold one or more times without prior notice to Borrower. A sale might result in a change in the entity (known as the “Loan Servicer”) that collects Periodic Payments due under the Note and this Security Instrument and performs other mortgage loan servicing obligations under the Note, this Security Instrument, and Applicable Law. There also might be one or more changes of the Loan Servicer unrelated to a sale of the Note. If there is a change of the Loan Servicer, Borrower will be given written notice of the change which will state the name and address of the new Loan Servicer, the address to which payments should be made and any other information RESPA requires in connection with a notice of transfer of servicing. If the Note is sold and thereafter the Loan is serviced by a Loan Servicer other than the purchaser of the Note, the mortgage loan servicing obligations to

Borrower will remain with the Loan Servicer or be transferred to a successor Loan Servicer and are not assumed by the Note purchaser unless otherwise provided by the Note purchaser.

Neither Borrower nor Lender may commence, join, or be joined to any judicial action (as either an individual litigant or the member of a class) that arises from the other party's actions pursuant to this Security Instrument or that alleges that the other party has breached any provision of, or any duty owed by reason of, this Security Instrument, until such Borrower or Lender has notified the other party (with such notice given in compliance with the requirements of Section 15) of such alleged breach and afforded the other party hereto a reasonable period after the giving of such notice to take corrective action. If Applicable Law provides a time period which must elapse before certain action can be taken, that time period will be deemed to be reasonable for purposes of this paragraph. The notice of acceleration and opportunity to cure given to Borrower pursuant to Section 22 and the notice of acceleration given to Borrower pursuant to Section 18 shall be deemed to satisfy the notice and opportunity to take corrective action provisions of this Section 20.

21. Hazardous Substances. As used in this Section 21: (a) "Hazardous Substances" are those substances defined as toxic or hazardous substances, pollutants, or wastes by Environmental Law and the following substances: gasoline, kerosene, other flammable or toxic petroleum products, toxic pesticides and herbicides, volatile solvents, materials containing asbestos or formaldehyde, and radioactive materials; (b) "Environmental Law" means federal laws and laws of the jurisdiction where the Property is located that relate to health, safety or environmental protection; (c) "Environmental Cleanup" includes any response action, remedial action, or removal action, as defined in Environmental Law; and (d) an "Environmental Condition" means a condition that can cause, contribute to, or otherwise trigger an Environmental Cleanup.

Borrower shall not cause or permit the presence, use, disposal, storage, or release of any Hazardous Substances, or threaten to release any Hazardous Substances, on or in the Property. Borrower shall not do, nor allow anyone else to do, anything affecting the Property (a) that is in violation of any Environmental Law, (b) which creates an Environmental Condition, or (c) which, due to the presence, use, or release of a Hazardous Substance, creates a condition that adversely affects the value of the Property. The preceding two sentences shall not apply to the presence, use, or storage on the Property of small quantities of Hazardous Substances that are generally recognized to be appropriate to normal residential uses and to maintenance of the Property (including, but not limited to, hazardous substances in consumer products).

Borrower shall promptly give Lender written notice of (a) any investigation, claim, demand, lawsuit or other action by any governmental or regulatory agency or private party involving the Property and any Hazardous Substance or Environmental Law of which Borrower has actual knowledge, (b) any Environmental Condition, including but not limited to, any spilling, leaking, discharge, release or threat of release of any Hazardous Substance, and (c) any condition caused by the presence, use or release of a Hazardous Substance which adversely affects the value of the Property. If Borrower learns, or is notified by any governmental or regulatory authority, or any private party, that any removal or other remediation of any Hazardous Substance affecting the Property is necessary, Borrower shall promptly take all necessary remedial actions in accordance with Environmental Law. Nothing herein shall create any obligation on Lender for an Environmental Cleanup.

NON-UNIFORM COVENANTS. Borrower and Lender further covenant and agree as follows:

22. Acceleration; Remedies. Lender shall give notice to Borrower prior to acceleration following Borrower's breach of any covenant or agreement in this Security Instrument (but not prior to acceleration under Section 18 unless Applicable Law provides otherwise). The notice shall specify: (a) the default; (b) the action required to cure the default; (c) a date, not less than 30 days from the date the notice is given to Borrower, by which the default must be cured; and (d) that failure to cure the default on or before the date specified in the notice may result in acceleration of the sums secured by this Security Instrument, foreclosure by judicial proceeding and sale of the Property. The notice shall further inform Borrower of the right to reinstate after acceleration and the right to assert in the foreclosure proceeding the non-existence of a default or any other defense of Borrower to acceleration and foreclosure. If the default is not cured on or before the date specified in the notice, Lender at its option may require immediate payment in full of all sums secured by this Security Instrument without further demand and may foreclose this Security Instrument by judicial proceeding. Lender shall be entitled to collect all expenses incurred in pursuing the remedies provided in this Section 22, including, but not limited to, costs of title evidence.

23. Release. Upon payment of all sums secured by this Security Instrument, Lender shall discharge this Security Instrument. Borrower shall pay any recordation costs. Lender may charge Borrower a fee for releasing this Security Instrument, but only if the fee is paid to a third party for services rendered and the charging of the fee is permitted under Applicable Law.

24. Certain Other Advances. In addition to any other sum secured hereby, this Security Instrument shall also secure the unpaid principal balance of, plus accrued interest on, any amount of money loaned, advanced or paid by Lender to or for the account and benefit of Borrower, after this Security Instrument is delivered to and filed with the Recorder's Office, _____ County, Ohio, for recording. Lender may make such advances in order to pay any real estate taxes and assessments, insurance premiums plus all other costs and expenses incurred in connection with the operation, protection or preservation of the Property, including to cure Borrower's defaults by making any such payments which Borrower should have paid as provided in this Security Instrument, it being intended by this Section 24 to acknowledge, affirm and comply with the provision of § 5301.233 of the Revised Code of Ohio.

BY SIGNING BELOW, Borrower accepts and agrees to the terms and covenants contained in this Security Instrument and in any Rider executed by Borrower and recorded with it.

Witnesses:

 _____ (Seal)
 - Borrower

 _____ (Seal)
 - Borrower

[Space Below This Line For Acknowledgment] _____

Judicial Foreclosure Procedure

When a borrower is in **default** on a loan, the lender *accelerates the due date of the debt to the present and gives the debtor notice of default, demanding the full loan balance be paid at once*. If the debtor fails to do so, the lender files a lawsuit, called a foreclosure action, in a court of jurisdiction where the land is located. There are some differences in how foreclosure proceedings progress, depending on the state and county in which the action takes place. We'll look at one scenario that's typical of foreclosure proceedings, but keep in mind there may be variations in your jurisdiction.

Under a **foreclosure action**, the *court determines whether the lender is rightfully owed the money and the debtor is in default*. If the court finds in favor of the creditor, the creditor takes ownership and a judge will issue an order of execution directing an officer of the court, usually the county sheriff, to seize the property. If the creditor chooses to sell, the public is notified of the place and date of the sale via advertising that runs for a specified number of weeks in a newspaper circulated in the county. On the sale date, a public auction is held at the courthouse where anyone can bid on the property. The minimum bid is generally a set percentage of the appraised value (two-thirds is a common figure), as determined by three disinterested appraisers. (The minimum bid requirement is set by law to protect whatever equity the debtor may have in the property, since a bidder can't simply get a bargain by paying just the mortgage balance.) The property is sold to the highest bidder, with proceeds used to pay costs of the sale and to pay off the mortgages and liens. Any **overages** remaining after all debts, liens, expenses, and costs related to the property are paid go to the debtor.

If the property does not bring enough money at the sale to pay off the mortgage, the creditor may be able to obtain a **deficiency judgment**, which is *a court order stating that the debtor owes money to the creditor when the collateral property does not bring enough at a foreclosure sale to cover the entire loan amount, accrued interest, and other costs*. The deficiency judgment is a personal judgment against the debtor that creates a general, involuntary lien against all real and personal property.

While this was a simple example, note that in today's marketplace, foreclosure procedures are undergoing challenges and modifications by both state governments and federal agencies. Make sure that you stay current with the practices and legal issues in the jurisdictions where you do business.

Redemption

Debtors may be able to redeem (save) their property from the time a *notice of a pending legal action*, called a **lis pendens**, is filed until the confirmation of the foreclosure sale. This is done by paying the court what is due, which may include court costs and attorneys' fees. In some states, this right to *save or redeem the property prior to the confirmation of sale* is called the **equitable right of redemption**. Some other states use the **statutory right of redemption**, which allows debtors to redeem themselves *after the final sale*. Once the redemption is made, the court will set aside the sale, pay the parties, and the debtor gains title to the property again.

One other option debtors have to avoid foreclosure is to make a voluntary conveyance, also called **deed in lieu of foreclosure**. With this action, *debtors still lose the property, but by conveying it voluntarily before final court action, they avoid having a foreclosure on their credit record*. After confirmation of sale, however, it is too late. Note that a lender is not obligated to accept a deed in lieu of foreclosure as full satisfaction of the debt and could still pursue a deficiency judgment.

Mortgage Lien Position

Lien position establishes the *order in which liens are paid off out of the proceeds of a foreclosure sale*. By law, real estate tax liens always have the highest priority and get paid first, followed by the first recorded lien. Then if there's money left, the second lien gets paid, and so on. Once the funds are exhausted, liens in a later position get nothing.

A **first mortgage** is a *security instrument with a first lien position*. As such, a first mortgage almost always has priority over all other mortgages, meaning the first mortgage holder is paid first in the event of a foreclosure sale.

A **second mortgage** is a *security instrument in a second lien position*. A second mortgage may be used to help buy the property (e.g., a small loan from the seller), or a second mortgage might be taken out later (e.g.,

a home equity loan) to generate additional funds from the owner's accumulated equity in the property for repairs, college tuition, or for some other purpose. Although property is still used as security, the second mortgage lender is in a riskier position because a first mortgage gets paid first out of foreclosure proceedings. If nothing is left, the second mortgage holder gets nothing.

Generally speaking, *any mortgage in a higher lien position* is said to be a **senior mortgage**, so a first mortgage is always a senior mortgage. A **junior mortgage** is *any mortgage with a lower lien position than another*. Thus, a second mortgage is a junior mortgage to a first mortgage, but a second mortgage is a senior mortgage to a third mortgage.

It's important to note that a mortgage would not necessarily be the first recorded lien on a property, however. For example, if someone purchases a new home from a builder who did not pay all of the subcontractors or suppliers prior to the borrower purchasing the home, any lawsuit for collection from the builder may relate back to when the work was commenced, which puts the mechanic's or materialman's lien ahead of the lender.

Subordination Agreement

In some situations, the parties may desire that a later recorded instrument have priority over an earlier recorded instrument. This is common in construction financing, for example. Because of the high-risk nature of construction loans, construction lenders frequently refuse to lend any money unless they can be assured of a first lien position. Since the developer, in many cases, has already purchased the land on some sort of deferred payment plan, there is often a security instrument (mortgage, trust deed, or land contract) that has already been recorded. For the later construction loan mortgage to take priority over the earlier recorded mortgage instrument on the land, the first lender would file a **subordination agreement** in the public record that permits the second lien holder to be in first lien position.

Another example is where a property owner has a junior mortgage, such as a home equity line of credit, and wants to refinance his first mortgage but keep the line of credit open. The holder of the junior mortgage would file a subordination agreement that gives the new mortgage priority, even though it was recorded later.

Typical Clauses in Finance Instruments

Various clauses are used in mortgages to give certain rights to the lender or borrower. Many of these clauses can be found in the promissory note or security instrument, and often they appear in both.

Acceleration Clause

An **acceleration clause** *gives the lender the right to declare the entire loan balance due immediately because of borrower default or for violation of other contract provisions*. Most promissory notes, mortgages, trust deeds, and land contracts contain an acceleration clause allowing the lender to accelerate the debt upon default as defined in the contract. This is important to lenders because, upon default, they want to be able to make all payments due without having to file a separate action for each missed payment.

The actions that constitute default are defined in the contract. A debtor who misses one payment may discover next month that, not just two payments are due but rather, the entire loan balance is due because of the missed payment. Most lenders, though, will wait until payments are delinquent at least 90 days before enforcing an acceleration clause that appears in the mortgage or note.

Alienation Clause

An **alienation clause** in a contract *gives the lender certain stated rights when there's a transfer of ownership in the property*. It may also be referred to as a **due on sale clause**. This is designed to limit the debtor's right to transfer property without the creditor's permission. Depending on the actual wording of the clause (that's why lawyers are important), alienation may be triggered by a transfer of title, by transfer of a significant interest in the property, or even by abandonment of the property. Transfer of a significant interest can be construed as an obvious long-term lease, but often is also interpreted to cover a lease with an option to buy or a land contract.

On sale or transfer of a significant interest in the property, the lender will often have the right to accelerate the debt (here called a due on sale clause), change the interest rate, or charge a hefty assumption fee. Adjustable rate mortgage (ARM) loans seldom have an alienation clause that calls for an interest rate change since the rate can already be adjusted under the original contract. An ARM loan may have other alienation provisions, however, such as an assumption fee. The lender may choose which, if any, options stated in the contract it chooses to enforce. This is true for most conventional loans. Although FHA and VA loans cannot, technically, have alienation clauses, they still attempt to restrict transfers in other ways, such as by reserving the right to approve a new debtor who will take over an FHA or VA loan.

Defeasance Clause

A **defeasance clause** is a clause in a legal document that states that in the event a stated condition has been fulfilled, the document becomes null and void. This clause can appear in contracts or mortgages. With a mortgage, for example, once the borrower has repaid the debt, the mortgage is cancelled and the mortgagor can redeem title to the property. This clause is more likely to be found in title theory states where title is transferred to the lender until the debt is repaid.

Partial Release, Satisfaction, or Reconveyance Clause

A **partial release, satisfaction, or reconveyance clause** in a contract obligates the creditor to release part of the property from lien and convey title to that part back to the debtor once certain provisions of the note or mortgage have been satisfied. Usually, this occurs after a certain percentage of the mortgage balance has been paid. This is an important clause that appears in many blanket mortgages and some construction mortgages so the developer or builder can sell off completed homes with clear title before having to pay back the entire amount borrowed for the entire development project. Also, if the land is bought with a mortgage, construction financing is much easier to obtain later when the builder owns part of the land free of liens.

Case in Point

A builder bought five acres of land with a contract that had a partial release clause. As per the contract, one acre of land would be released with clear title to the builder for each 20% of the note amount that was paid. This would allow the builder to build a house on this one-acre parcel and sell it free and clear.

Prepayment Clause

A **prepayment clause** in a contract gives the lender the right to charge the borrower a penalty for paying off the loan early, such as when refinancing a loan. While the time periods and amount of the penalty may vary considerably, the basic effect of a prepayment clause is to charge the debtor extra money to make up for the interest income the lender loses when the debtor pays the loan early. An example might be a prepayment clause that calls for the debtor to pay an additional 3% of the loan amount if more than 20% of the principal is repaid during the first five years of the loan. This type of clause may be seen in a conventional loan, but it is prohibited in FHA or VA loans.

Title XIV of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, designated as the Mortgage Reform and Anti-Predatory Lending Act, prohibits prepayment penalties on residential mortgage loans other than “qualified mortgages,” which are those with points and fees that do not exceed 3% of the loan amount or that do not have adjustable rates and do not result in negative amortization (§ 1414).

Other Mortgage Covenants

In addition to the typical clauses discussed that appear frequently in real estate mortgages, there are also a number of covenants. **Covenants**, simply, are *promises*. Covenants can appear in deeds, mortgages, or any other document. Typical covenants can compel or prevent certain actions by the property owner or uses for the property.

Typical covenants in mortgages that the property owner must sign include provisions protecting the lender's security interests in the property. These covenants include such things as the property owner promising to keep the property in good condition and repair; not committing **waste**, which is damaging or diminishing the value of the property in any way; promising to keep fire, hazard, and flood insurance in force on the property; and agreeing to pay taxes and other assessments on time. Failure to keep any of these promises or covenants can be cited in the mortgage or note as causing the borrower to be in default.

There are, of course, a number of other clauses and covenants important to typical mortgages. Borrowers should make sure they understand them, and should be encouraged to consult legal counsel before entering into a mortgage.

Types and Features of Mortgages

There are actually many different types of mortgages, and they all share many characteristics and have the same origins. The history of the actual word “mortgage” is very interesting. “Mort”—from the Latin—means “death,” while “gage” means something deposited as a pledge of performance. So the word mortgage literally means a “dead pledge” in that the property is forfeit or dead to the borrower if the loan isn't repaid, and the pledge or conveyance is dead once the loan is repaid.

Although mortgages are primarily security devices used to collateralize real estate loans, the word mortgage is often prefaced with adjectives that describe the particular function the mortgage is serving, or the nature of the circumstances surrounding its use. For example, a construction mortgage is a mortgage used to secure a construction loan; a blanket mortgage secures a loan with two or more parcels of land as collateral, etc.

✓ **Note:** Some mortgage loans can be more than one type of mortgage loan at the same time, plus some share many different mortgage features. For example, a borrower can have a conventional mortgage loan that is a first mortgage (and thus a senior mortgage), and this same mortgage can also be an adjustable rate mortgage that is a construction mortgage. Of course, some of the mortgage types and features are mutually exclusive—a construction mortgage can't also be a reverse equity mortgage.

Purchase Money Mortgage

The term **purchase money mortgage** generally describes *any mortgage given by a buyer to a lender or a seller to secure part or all of the money that's borrowed to purchase property*. When a seller takes part of the purchase price as a mortgage to help the sale, it may also be known as a **soft money loan**, because the borrower receives credit toward the purchase instead of actual cash. A purchase money mortgage can be a first mortgage or a junior mortgage, depending on its lien priority.

Refinance Mortgage

A **refinance mortgage** is one *where the borrower replaces the current mortgage with a new loan*. This can be a way for a borrower to simply get a better interest rate or other terms on a new loan compared to the original mortgage, for example, to lower the interest rate, change an adjustable rate to a fixed rate, change a 30-year loan to a 15-year loan, combine multiple mortgages into one, or remove private mortgage insurance. This transaction could be a no cash-out refinance or a cash-out refinance. With any refinance, the mortgage loan originator should be able to show a net tangible benefit to the borrower.

Home Equity Loan, Home Equity Line of Credit

A home equity loan or home equity line of credit (HELOC) is a loan *secured by a mortgage on one's principal residence*. A **home equity loan** is typically a **closed-end** loan that offers a fixed amount of money that can be repaid with regular payments over a fixed term. A **home equity line of credit** is a type of **open-end** loan in which a borrower is granted a specific credit limit from which he or she can draw and pay back principal only as it is used. As the balance is paid down, the principal is available to be used again. HELOCs usually have

two phases: A draw period during which borrowers commonly pay interest only, and a repayment period during which payments are generally amortized. Usually, these financing vehicles attach a junior mortgage to the property.

Blanket Mortgage

A **blanket mortgage** covers more than one parcel of land or lot, and is usually used to finance subdivision developments. These loans usually have a **partial release clause**, allowing the borrower to pay a certain amount to release some of the lots with the mortgage continuing to cover the remaining lots. Using a subdivision example, a builder may initially have one mortgage covering the entire acreage but, by paying down a certain percentage of the loan, the builder can sell off completed home lots.

Bridge Mortgage

A **bridge mortgage** occurs *between the termination of one mortgage and the beginning of the next*. When the next mortgage is taken out, the bridge mortgage is repaid. Bridge mortgages are designed to be temporary, and are used most commonly for construction financing. A less common use for a bridge mortgage is for someone buying a new home before selling the old one.

Open-End Mortgage

An **open-end mortgage** allows the borrower to request additional funds from the lender, usually up to a certain pre-defined limit. In most cases, lenders will not advance funds in excess of the original principal balance of the loan or that exceed a predetermined loan-to-value. As an example, a borrower obtains an open-end mortgage to buy a home. Under the terms of the mortgage, he may borrow additional funds over the term of the loan as long as the unpaid principal does not exceed 80% of the appraised value of the property used as collateral. An example of another type of open-end loan is a home equity line of credit, in which a borrower can borrow, repay, and borrow again up to the pre-defined limit.

Don't confuse an open-end mortgage with an **open mortgage**, which is a term used to describe a mortgage that may be repaid at any time without penalty.

Package Mortgage

A **package mortgage** includes personal property, like appliances, in the property sale and all are financed together in one contract. With package mortgages, the personal property also serves as collateral for the loan. A common use for this type of mortgage is to buy a furnished condominium, where the loan and mortgage documents may also recite appliances and/or furniture as part of the transaction. More commonly, lenders obtain a separate financing statement or UCC filing to claim covered personal property as collateral.

Reverse Mortgage

A **reverse mortgage** allows qualified homeowners age 62 or older to convert equity in the home into a monthly cash stream or line of credit that may be used by the borrower for investment, repairs, payment of debt, or other purposes as the borrower sees fit. The borrower must have a substantial amount of equity in the home to make this option viable. Unlike a conventional mortgage, the borrower is not required to make payments against a reverse mortgage during the life of the loan. In most cases, the mortgage must be repaid when the home is sold, the borrower does not occupy the home for 12 consecutive months, or the borrower dies. The borrower may also pay off a reverse mortgage at any time or refinance it.

Equity Participation Mortgage

An **equity participation mortgage** permits the lender to share part of the earnings, income, or profits from a real estate project. This is usually in addition to collecting principal and interest payments on the loan. For example, the lender may receive 5% of gross rents. This is done mostly for commercial real estate projects.

Wraparound Mortgage

The term **wraparound mortgage** is used to describe a financing arrangement in which *an existing loan on a property is retained while the lender gives the borrower another, larger loan*. For example, this arrangement could be used in lieu of traditional refinancing where a lender makes a second loan to a borrower, leaving the first loan intact. The borrower pays the wraparound lender a single payment on the combined principal. If the wraparound lender is not the original lender, then the wraparound lender makes payments on the original mortgage to the first mortgage lender. For example, a homeowner wants to borrow \$40,000. He has an existing mortgage with a balance of \$20,000 at 4%. A second lender gives him a wraparound mortgage for \$60,000 at 5%. The borrower makes payments on the \$60,000 loan to the second lender, who must make payments to the first lender for the \$20,000 balance of the first loan. The benefit for the second lender in this arrangement is that it earns a return not only on the money it advanced at 5%, but also on the difference between the rate it is charging the borrower and the rate at which it is repaying the first mortgage. While such an arrangement may be more convenient for the borrower, it can place him at greater risk, since he must depend on the second lender to make timely payments to the first lender. Failure of the second lender to do so could trigger a default and foreclosure action.

Construction Mortgage

A **construction mortgage**, also called an interim loan, is *a temporary loan used to finance the construction of improvements and buildings on land*. Generally, an appraiser will value the property for a construction loan by evaluating the building plans and specifications, completing a “subject to” appraisal. When construction is complete, the appraiser verifies that plans and specifications have been met and the original opinion of value is valid; then the loan is replaced by a permanent amortizing loan, called a **take out loan**. New construction can take as long as a year to complete; therefore, some contracts may include **extended rate locks**.

Construction loans can be profitable, but lenders regard them as risky. Thus, not only do they charge high interest rates and loan fees on construction loans, they also closely supervise the disbursement of funds to ensure that projects are completed. There’s always the danger that a borrower will overspend and exhaust the loan funds before construction is complete. If the borrower doesn’t have money to finish a project, the lender is left with a partially completed project that can’t be sold easily in its existing state—with a very real possibility of foreclosure. To protect themselves against this problem, lenders use plans for **disbursing construction loan proceeds** to guard against overspending by the borrower. Three common disbursement plans are fixed disbursement plan, voucher system, and warrant system.

Disbursement

A **fixed disbursement plan** *pays a percentage of funds at a set time*. A series of predetermined disbursements, called **obligatory advances**, are paid out at various stages of construction. For example, the loan agreement may state that the lender will release only 10% of the funds when a project is 20% complete, with future draws of 20% each time construction progresses 20% more toward completion.

First Release/Draw	10% of Loan	Project 20% complete
Second Release/Draw	20% of Loan	Project 40% complete
Third Release/Draw	20% of Loan	Project 60% complete
Fourth Release/Draw	20% of Loan	Project 80% complete
Fifth Release/Draw	20% of Loan	Project 100% complete

Lenders often hold the final 10% (or more) of the loan proceeds until the lien period has expired to protect against unpaid mechanic’s liens, which could affect the marketability of the property. If a valid mechanic’s lien is recorded, the construction loan agreement usually allows lenders to pay it from the part of the loan not disbursed.

- **Voucher System.** The contractor or borrower must pay his or her own bills, and then submit the receipts to the lender for reimbursement.
- **Warrant System.** The lender directly pays bills presented by the various suppliers and laborers on a project.

Permanent Construction Loan

A **permanent construction loan** is a *special type of construction loan where there is only one loan and one closing, with no take out loan*. There is a fixed disbursement schedule for loan funds, and the loan automatically converts to a permanent first mortgage when construction is finished.

GRADUATED PAYMENT MORTGAGE (GPM)

A **graduated payment mortgage** (GPM) is actually a **specialized payment structure** that *allows the borrower to make smaller payments in the early years of a mortgage*. The lower payments in the early years of a mortgage structured in the note as a GPM are not sufficient to cover the interest due on the loan, and so the unpaid interest is added to the loan balance, resulting in a scheduled period of **negative amortization**. At a predetermined point in the loan term, the payments escalate on a scheduled basis until they eventually reach the point in which they are sufficient to fully amortize the loan over the remainder of its term.

Chapter 5 Summary

1. **Finance instruments** are written documents establishing rights and duties of the parties in a transaction. **Promissory notes** are written promises to pay money. They're **negotiable instruments** and are freely transferable. The one promising to pay is called the **maker** of the note, usually the borrower. The one to whom payment is promised is called the **payee** (usually the lender), or payee's order, or to the order of the payee. There are four common note types: Straight note, installment note, installment note with balloon, and fully amortizing note. The rate that is used to amortize the mortgage loan and determine the monthly loan payments is known as the **note rate**.
2. **Security instruments** give a creditor the right to take ownership of collateral to satisfy the debt if the debtor doesn't pay as agreed; they require a debtor to **hypothecate** the property, which means to pledge it as collateral without giving up possession. Two types are trust deeds and mortgages.
3. **Trust deeds** (or deeds of trust) place legal title interest in the property into the hands of a third party as security for the payment of a note; they allow for non-judicial foreclosure in the event of default.
4. **Mortgages** create liens against property as security for debt. If in default, **judicial foreclosure** ensues: Notice of default; foreclosure action filed; creditor takes ownership; if selling, order of execution has sheriff sell property; advertising; and public auction (minimum bid based on percentage of appraised value, confirmation of sale to highest bidder, sheriff's deed issued.) Debtor has **equitable right of redemption** to regain property until confirmation of sale. Process is slow and expensive, but has court authority. The order of mortgage is important: A **senior mortgage** is any mortgage in a higher lien position; a **junior mortgage** is in a lower lien position. Property tax liens are always paid first.
5. Many clauses are common in real estate financing contracts. An **acceleration** clause lets the lender call the loan balance due if in default. A **prepayment** clause lets lenders charge a penalty for paying off a loan early. An **alienation** clause gives lenders some stated rights if the property is transferred (also called due on sale clause). A **defeasance** clause cancels a mortgage when it has been repaid. **Subordination** lets a later-recorded mortgage take priority over an earlier one. A **partial release** is when a part of property is released from the lien upon payment of part of the balance.
6. Mortgages are often prefaced by words describing its type or function. **Purchase money** mortgage—Seller or lender takes mortgage for part of purchase price. **Soft money** mortgage—Borrower gets credit instead of cash. **Hard money** mortgage—Borrower gets actual cash (e.g., cash-out refinance). **Bridge** mortgage—Temporary mortgage between two others and repaid with a later mortgage or proceeds from sale of security property. **Package** mortgage—Includes personal property. **Blanket** mortgage—For more than one land parcel. **Construction mortgage**—Temporary loan to finance construction of building improvements.

Chapter 5 Quiz

1. *A promissory note calling only for payment of interest during its term is a(n)*
 - A. amortizing note.
 - B. installment note.
 - C. negotiated note.
 - D. straight note.
2. *The clause that permits a lender to declare the entire unpaid balance on a loan due and payable at once on default of the borrower is a(n)*
 - A. acceleration clause.
 - B. defeasance clause.
 - C. escalation clause.
 - D. forfeiture clause.
3. *A clause that permits the lender to call the outstanding balance due and payable should the property be sold by the borrower is a(n)*
 - A. acceleration clause.
 - B. alienation clause.
 - C. balloon payment clause.
 - D. exculpatory clause.
4. *Which document accompanies the mortgage?*
 - A. abstract of title
 - B. contract of sale
 - C. deed
 - D. promissory note
5. *To foreclose a mortgage, the creditor*
 - A. files an attachment in the amount of the debt.
 - B. files a court action.
 - C. notifies the debtor of the default, waits ten days, publishes a notice of default in the paper, then claims a forfeiture.
 - D. notifies the trustee of default.
6. *A mortgage under which the debtor may re-borrow up to the original note amount under the same document is a(n)*
 - A. amortizing mortgage.
 - B. hypothecated mortgage.
 - C. open-end mortgage.
 - D. package mortgage.
7. *The type of mortgage that may provide the borrower with a monthly check instead of the borrower paying a monthly payment is known as a(n)*
 - A. blanket mortgage.
 - B. graduated payment mortgage.
 - C. interest only mortgage.
 - D. reverse mortgage.
8. *A builder finances the construction of an apartment building through a local bank. If money is released to the builder at various stages of construction, these payments are called*
 - A. acceleration advances.
 - B. obligatory advances.
 - C. release payments.
 - D. site drafts.
9. *The term "take out loan" is most closely associated with*
 - A. construction loans.
 - B. junior loans.
 - C. loans against the land.
 - D. Truth in Lending requirements.
10. *Which term describes the process by which a borrower pledges property as security for a loan without giving up possession of it?*
 - A. defeasance
 - B. hypothecation
 - C. redemption
 - D. subordination

