

# An Introduction to Real Estate

## Focus of this Chapter

This chapter introduces the basic concepts of real and personal property, introduces the rich and complex world of real property, and explains the various categories of real property.

## Chapter Learning Objectives

After completing this chapter, you should be able to:

- Explain the differences between real and personal property
- Explain the economic characteristics of real property
- Describe the real estate market
- List and explain the various classifications of real property
- Explain the differences between residential, commercial, and industrial property.

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## INTRODUCTION

In this chapter we examine the basic concepts of real property. We first examine how real property differs from personal property, and then dig deeper into the issues by showing how the unique qualities of real property are revealed in a wide variety of ways, from how land is classified to how title to real property is conveyed from a seller to a buyer.

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## REAL PROPERTY VERSUS PERSONAL PROPERTY

All property can be divided into two classifications: real property or personal property. Although the original meanings of these terms had special relevance

in regard to how a case was brought — and the court in which the action could be brought — these days the differences have more to do with the way that ownership interests are transferred, as well as other differences. In the modern era real property refers to land — and anything permanently attached to land. Personal property refers to all other types of property. As such, real property refers to the land, houses, trees, and any other permanent structures. Personal property refers to non-real estate items, including everything from apples to automobiles.

## ISSUE AT A GLANCE



**“Real property” refers to land and anything permanently attached to land.**

The reason that the law makes a distinction between these two types of property is that the classification affects many of the rights and legal remedies available to the owners. For one thing, the way that ownership is transferred in real estate is different from the way it is transferred in personal property. We will see time and again that there is a great deal of symbolism in real estate transactions. In Chapter 2, we will see that the modern real estate transaction still holds many of the same features used in the Middle Ages and earlier. That is particularly true when it comes to transferring title to real property. For personal property, possession often equates to ownership. Bills of sale, receipts, and other indicia of title are helpful in proving ownership of personal property, but possession is the best way. In fact, the old common law rule that “possession is nine-tenths of the law” is a maxim that applies to personal property, not real property. “Possession” in the context of real property obviously means something different than the ability to carry the property around with you.

## ISSUE AT A GLANCE



**Real property ownership interests are transferred in a different way than ownership interests in personal property.**

### **Statute of Frauds:**

Originally enacted in England and later adopted in all American states, this statute requires certain types of contracts to be in writing before they can be enforced. Typical contracts covered by the Statute of Frauds include contracts to answer for the debt of another and transactions involving real estate.

Real property ownership interests are transferred by deed. The deed is the evidence of ownership. Delivery and acceptance of the deed are the physical acts that transfer ownership from one person to another. Another difference between real property and personal property is taxation. Taxes are assessed differently on personal property and real property. Taxes on personal property usually are assessed by sale price, while taxes on real property are based on the assessed value. We explore these and many other differences in later chapters.

The transfer of ownership interest in real estate is required to be in writing under the **Statute of Frauds**. However, most transfers of personal property are not required to be in writing. We explore the Statute of Frauds in greater detail in Chapter 8.

PERSONAL PROPERTY	REAL PROPERTY
Usually refers to mobile items	Always refers to land
Often taxed on sale price	Often taxed on assessed value
Ownership is evidenced by possession	Ownership is evidence by deed
Statute of Frauds usually does not apply	Statute of Frauds applies to almost all transactions

**FIGURE 1-1**

Differences Between Real Property and Personal Property

Knowing how to classify property as real or personal also has a practical consideration: In a real estate transaction, there is no need to refer to the specific items of real property that are being sold. The house, trees, soil, and attached garage are never mentioned in the deed. The seller may remove personal property items, such as furniture, beds, and unattached appliances, unless the parties have specifically negotiated the sale of these items of personal property. The sale of real property involves the sale of all items that are permanently attached to the land, which is why there is no need to list them. Personal property, on the other hand, must be specifically listed as to all items for which title is changing hands.

In the past, the difference in classification between real and personal property also had an effect on probate law. Real property interests were transferred to heirs in different ways than personal property. Although many of those probate rules have changed, there are still important differences that arise in transferring title through an estate proceeding.

## A. WHAT MAKES REAL PROPERTY SO UNIQUE?

Real property is a unique and specialized area of law for several reasons. As we will see throughout this chapter, real property has its own set of rules for selling, buying, mortgaging, and investing. Real property also has unique physical attributes. For one thing, real estate occupies a fixed point on the globe. Rivers may change course, houses may be torn down, but the underlying land remains where it is. Land that is submerged under a lake is still there, if inaccessible.

Real property has its own set of laws, statutes, cases, and judicial interpretations that make it an entirely separate branch of law. Many attorneys devote their careers to this one area of law. It is as specialized as criminal defense, trademark, and labor law. Attorneys and paralegals can spend decades in the practice of real property law and still not learn all its aspects. During the course of this book, we discuss many of the legal implications that arise from real property, from easements to encroachments, from mortgages to metes and bounds descriptions, while learning a great deal about property law in all its rich diversity.

Real property is also unique because of the financial arrangements used to purchase it. Later, we examine the issue of deeds of trust and mortgages and the legal impact of these financing instruments on real estate ownership.

### Sidebar

*Most states have their own statewide real estate treatise. Usually written by a noted scholar or attorney, a real estate treatise is a great source of information about real property law in a particular state. It provides not only legal background but also practical applications. You should locate and acquire your own copy of the real property treatise for your state.*

## B. PHYSICAL CHARACTERISTICS OF LAND

Real property has several distinctive characteristics that separate it from personal property. As mentioned above, land occupies a specific point on the globe. Unlike personal property, land is fixed and immovable; it cannot be relocated. For this reason, it is the perfect vehicle for assessing taxes. (In Chapter 14, we explore how real estate taxes are assessed). Another physical characteristic of real estate is that no two pieces of land are identical. Each one is unique, with its own special characteristics and chain of ownership. Also, because land is located within different jurisdictions, the rules governing real estate transactions vary considerably. Land falls under the law of whatever state it happens to be located in. A single individual can own land in any number of different states and each parcel falls under different rules and statutes. An owner cannot claim, that simply because he is the owner of all the tracts, that they should all fall under one set of rules.

This fact controls some of the rules regarding lawsuits involving real estate. There is a specific term for this type of jurisdiction — **in rem jurisdiction**. This is a court's power to enter decisions and rulings simply because the land involved happens to be within the court's geographic limits. In most lawsuits, the court's jurisdiction is based on **personal jurisdiction**, that is, power over the people involved in the suit. However, in some lawsuits, a court acquires jurisdictional power simply because a tract of land lies within its geographic boundaries. We explore many of these jurisdictional questions in Chapter 4.

### In rem jurisdiction:

A court's power to render decisions based on the location of the land within the court's geographic boundaries.

### Personal jurisdiction:

A court's power to render decisions based on an individual's personal connections and interactions within the court's geographic boundaries.

## Sidebar

*There is at least one major movie star who earns more money every year from his real estate investments than the millions he makes on making action films.*

## C. ECONOMIC CHARACTERISTICS OF LAND

In addition to the unique physical characteristics, land also has some interesting economic characteristics. For one thing, land is an excellent investment. In the past, a person's wealth was measured by the extent of his real estate holdings. Land ownership continues to be an important source of investment income for many individuals.

Land also offers some economic benefits to persons who is not wealthy. In fact, one of the best economic benefits of land ownership is the tax consequences of home ownership. In Chapter 4, we explore how a homeowner earns a substantial tax benefit from being able to deduct mortgage interest payments from his yearly income tax return.

Another interesting aspect of real estate is that unlike almost all other purchases, it generally appreciates in value. Because there is a fixed supply of land, and an ever-growing population, the realities of supply and demand put upward pressure on real estate prices. In many areas of the country, the value of a person's home and land increases about 6 percent a year. This makes land an attractive investment even for

**FIGURE 1-2**

Physical Characteristics of Land

### Land is

- Permanently fixed and immovable
- Unique; no two pieces of land are exactly the same

- Used by local governments for assessing taxes

Specified owner-occupied units	55,212,108	100.0
<b>VALUE</b>		
Less than \$50,000	5,457,817	9.9
\$50,000 to \$99,999	16,778,971	30.4
\$100,000 to \$149,999	13,110,384	23.7
\$150,000 to \$199,999	8,075,904	14.6
\$200,000 to \$299,999	6,583,049	11.9
\$300,000 to \$499,999	3,584,108	6.5
\$500,000 to \$999,999	1,308,116	2.4
\$1,000,000 or more	313,759	0.6
Median (dollars)	119,600	(X)
<b>MORTGAGE STATUS AND SELECTED MONTHLY OWNER COSTS</b>		
With a mortgage	38,663,887	70.0
Less than \$300	255,243	0.5
\$300 to \$499	2,149,992	3.9
\$500 to \$699	4,943,283	9.0
\$700 to \$999	9,612,512	17.4
\$1,000 to \$1,499	11,679,988	21.2
\$1,500 to \$1,999	5,555,203	10.1
\$2,000 or more	4,467,666	8.1
Median (dollars)	1,088	(X)
Not mortgaged	16,548,221	30.0
Median (dollars)	295	(X)

**FIGURE 1-3**

Value of Homes in 2000

### Profile of Selected Housing Characteristics. U.S. Census 2000.

those of a moderate income. However, like any other item, land can also decrease in value. Still the price fluctuations of land are relatively minor, especially when you compare the long-term prices of real estate to other commodities.

In recent years, falling interest rates have also encouraged people to refinance their homes. This has the advantage of allowing an owner to receive some of the **equity** value in a home as cash that can be spent on home improvement, or used to finance college tuition, vacations, or any number of projects.

Equity itself is another aspect of the economic characteristics of land ownership. When we say that a person has equity in his home, what we are actually saying is that there is a difference between what the person owes on the home and what the home (and land) are actually worth.

#### Equity:

A homeowner's value in property once the amount owed on the property is subtracted from its current fair market value.

Juan purchased his home 15 years ago and has been making regular monthly mortgage payments on it. His original loan amount was for \$150,000. In the past 15 years, he has lowered the balance of the loan to \$85,000. However, because Juan's house has steadily been appreciating in value over the years, the house is now worth \$220,000. How much equity does Juan have?

Answer: Juan has \$135,000 in equity. How do we arrive at this amount? Subtract the amount that Juan owes on the house from the current value ( $\$220,000 - \$85,000 = \$135,000$ ).

Although this appears to be a simple paper gain, Juan can actually borrow against his equity. He can apply for a second mortgage and borrow against this "paper value" for real money.

#### Example 1-1



## THE REAL ESTATE MARKET

There is a market for land, just as there is a market for commodities or goods. The real estate market has its own rules and regulations. It also has participants, such as brokers, agents, loan correspondents, and attorneys and paralegals, to name just a few. We explore the role played by these participants as we develop the concepts of real estate in later chapters.

We begin our discussion of the real estate market with a straightforward example.

### Example 1-2

Maria and Vern Seller have outgrown their house and want to put it up for sale. They contact Good & Better Real Estate Agency to discuss their options. Alvin Agent tells them that if they sign a listing agreement with the agency, Good & Better will advertise their house for sale, put a sign in their yard, list the home in the Multiple Listing Service, and make every effort to give the house the best chance of being sold.

Maria and Vern decide to put their house up for sale and they list it with Good & Better. Bill Buyer sees the house listed and decides that he wants to purchase the home. He contacts Good & Better and gets the price particulars. Then he goes to a bank, meets with a loan officer, and arranges financing to purchase the home. Finally, he buys the home from the Sellers.

Although we have oversimplified the typical real estate transaction in Example 1-2, it gives us a starting point to discuss how the real estate market functions.

In any market there must be buyers and sellers. Maria and Vern are sellers and Bill is a buyer. Good & Better is acting for Maria and Vern to list the house for sale. In exchange for this service, Good & Better will receive a percentage of the total sale price (called a commission). The Sellers could have put their house up for sale on their own. For instance, they could have paid for an ad in the local newspaper, put a sign in their yard, and printed brochures to distribute to various places around the city, but they have decided that they would prefer to leave the job of marketing their home to professionals. Later, we will see that listing a home with a real estate agent brings certain advantages that are almost impossible for a single home seller to match.

When Bill Buyer decides to purchase the Sellers' home, he goes to a bank to borrow money. Most people who buy homes must obtain a mortgage because few people have that much ready cash on hand. The real estate market also includes banks and other lending institutions. The banks in turn rely on others to review a borrower's application, assess the possible risk of the transaction, and establish the actual value of the home.

Throughout this book, we examine not only the theoretical basis of real property, but also the day-to-day activities of real estate professionals. We will also see that, in many ways, the health of the real estate market is an indicator of the strength of the overall economy. Before we can delve into these topics, we must have a firm understanding of the various ways that real estate is classified.

## IV

## CLASSIFYING PROPERTY BY USE

One of the oldest and most easily understood methods of classifying property is by the use to which it is put. There are several different categories of property, including residential property, condominiums, mobile homes, manufactured housing, commercial property, and industrial and farm property.

However, before we set out these classifications, we first examine exactly how the term *land* is defined. For our purposes, we define land as including the grass, soil, trees, and anything else permanently affixed to the ground, including the soil underneath and the structures above. This includes the owner's air rights in the space above the property. With this working definition of land, we now examine specific subcategories of land.

<b>Total housing units</b>	<b>115,904,641</b>	<b>100.0</b>
<b>UNITS IN STRUCTURE</b>		
1-unit, detached	69,865,957	60.3
1-unit, attached	6,447,453	5.6
2 units	4,995,350	4.3
3 or 4 units	5,494,280	4.7
5 to 9 units	5,414,988	4.7
10 to 19 units	4,636,717	4.0
20 or more units	10,008,058	8.6
Mobile home	8,779,228	7.6
Boat, RV, van, etc.	262,610	0.2
<b>YEAR STRUCTURE BUILT</b>		
1999 to March 2000	2,755,075	2.4
1995 to 1998	8,478,975	7.3
1990 to 1994	8,467,008	7.3
1980 to 1989	18,326,847	15.8
1970 to 1979	21,438,863	18.5
1960 to 1969	15,911,903	13.7
1940 to 1959	23,145,917	20.0
1939 or earlier	17,380,053	15.0
<b>ROOMS</b>		
1 room	2,551,061	2.2
2 rooms	5,578,182	4.8
3 rooms	11,405,588	9.8
4 rooms	18,514,383	16.0
5 rooms	24,214,071	20.9
6 rooms	21,385,794	18.5
7 rooms	13,981,917	12.1
8 rooms	9,343,740	8.1
9 or more rooms	8,929,905	7.7
Median (rooms)	5.3	(X)

**FIGURE 1-4**

Total Housing Units in the United States

**Profile of Selected Housing Characteristics. U.S. Census 2000.**

## A. UNIMPROVED LAND

### Improvements:

Buildings, fences, barns, and other structures that add value to raw land.

### Unimproved land:

Raw land that contains no structures.

When land contains **improvements**, it means that it contains structures. **Unimproved land** has no buildings or other structures on it, so it is often referred to as raw land. Such property can be developed into any number of uses: homes, businesses, farms, or parks. Once land has been improved, it can be reclassified into residential, farm, commercial, industrial, or recreational. The categories are all based on the way in which the land is used.

ISSUE AT  
A GLANCE



“Unimproved land” has no structures.

## B. RESIDENTIAL PROPERTY

Property categorized as residential refers to land that has a structure designed to be used for personal living, such as a home. There are numerous subcategories of residential properties, including single and multi-family units, apartments, condominiums, mobile homes, and manufactured homes.

### 1. SINGLE-FAMILY HOMES

The category of single-family homes includes residential houses, duplexes (two family units sharing a single roof), triplexes (three family units), and four family homes (four family units). When more than four family units share a single roof, the law characterizes that arrangement as an apartment.

### 2. APARTMENTS

The technical definition of an **apartment** is a type of residential real estate consisting of five or more living units per building. In many large urban areas, there may be hundreds of apartments in any given complex. Apartments are popular because the residents have far less responsibility for maintaining the building, they generally have no responsibility for keeping up the grounds, and they do not require a large initial investment to move in. On the other hand, while apartment buildings can be a great financial investment for the owners, they provide few, if any, financial advantages for the residents. Apartment residents, or tenants, pay rent to the apartment owners in exchange for the use of the premises. We examine landlord-tenant law in greater detail in Chapter 7.

### 3. CONDOMINIUMS AND TOWNHOUSES

Condominiums and townhouses share many characteristics, but there are important differences that a legal professional should know.

### Apartment:

A leased residence containing more than five living units sharing a single roof or foundation.

### a. Condominiums

A **condominium** resembles an apartment, but is actually more like a hybrid between a home and an apartment. The tenant in an apartment does not have any ownership interests in the dwelling. He must seek permission from the owner before making changes to the interior, and is not allowed to make any changes to the exterior. A condominium gives the resident an ownership interest in the interior of the dwelling, but no rights to the exterior. Regarding the interior, the resident has the same legal rights as a homeowner. Condominiums can be sold just like homes, but the only thing that is being sold is what is inside the four walls. No actual land is transferred in the sale of a condominium. The owner of a condominium receives the same favorable tax treatment as a homeowner, but does not have the responsibility of exterior upkeep and maintenance. Condominium owners must pay yearly fees to homeowners' associations who contract with maintenance firms to take care of yard work and to maintain the various facilities. Condominiums often have pool and gym facilities and are very attractive to people who do not want the burden of home maintenance, yet wish to receive the financial benefits of home ownership.

Condominiums typically have common areas that are owned and maintained by a homeowners' association. These common areas consist of the sidewalks connecting the various units and the amenities, such as swimming pools, tennis courts, and walking trails. A condominium owner usually pays mandatory annual dues to the homeowners' association to defray the cost of maintaining these public areas.

### b. Townhouses

While condominium owners have legal rights only to the inside of their individual units, **townhouse** residents own the entire unit, both the interior and exterior walls. They also own the land that the townhouse is situated on. In many states, there are no specific statutes that govern the creation of townhouses. Instead, in most states, the same rules and statutes that govern single-family homes control townhouses.

**Condominium:**

A form of real property in which the owner has full title to the interior, but not the exterior, of the structure.

**Townhouse:**

A form of real property in which the owner has title to both the interior and exterior of a structure that resembles an apartment instead of a traditional residence.

## 4. COOPERATIVES

Cooperatives, unlike condominiums and townhouses, are often large tracts of land, or working farms in which several persons have an ownership interest. Unlike condominiums, both interior and exterior portions of the property are owned jointly by all the members of the cooperative. These may also include large buildings owned by members.

## 5. MOBILE HOMES

Mobile homes are usually considered to be personal property and not real property. This classification carries with it some important consequences. The owner of a mobile home does not receive the same kind of favorable tax treatment as does a homeowner. The mobile home owners cannot, for instance, "write off" their mortgage interest payments for the year on their annual income tax return. Mobile homes can be reclassified as real property, but usually only after removing the

**FIGURE 1-5**

Percentage of  
Homeownership Rates,  
1930-2000

**HOMEOWNERSHIP RATES**

	2000	1990	1980	1970	1960	1950	1940	1930
<b>United States</b>	66.2%	64.2%	64.4%	62.9%	61.9%	55.0%	43.6%	47.8%

U.S. Census 2000, Census of Housing

wheels of the unit and permanently affixing it to the ground. Because houses are by their very nature permanently attached to the real estate — thus becoming reclassified as real estate — anything that a mobile home owner can do to duplicate this process will push the mobile home away from a personal property classification toward a real property classification.

When a mobile home is considered to be personal property, it usually falls under the jurisdiction of the Uniform Commercial Code, not state real property laws. The Uniform Commercial Code governs transactions in personal property, and has very specific rules about the transfer of ownership, shipment of goods, and other issues. These rules differ from real property rules in significant ways. Some state decisions actually hold that a mobile home is a form of motor vehicle, not real estate.<sup>1</sup> In order for a mobile home to change from a classification of personal property to real property, several actions must take place. Among them are:

- The homeowner establishes the mobile home on the land with an obvious intent to make it permanent.
- The homeowner clearly intends to treat the mobile home as real property.
- The homeowner pays taxes on the mobile home as though it were a house.

## 6. MANUFACTURED HOUSING AND “KIT” HOMES

In recent years there has been a huge upswing in the construction of manufactured housing. Manufactured homes are homes in which all or some of the fabrication occurs away from the actual home site. In prior decades, manufactured housing fell into the same category as mobile homes. However, because these newer houses are actually permanently affixed to the real estate, and are never intended to be movable, most states have abolished the distinction between manufactured homes and traditional homes that are constructed entirely on the site.

## C. COMMERCIAL PROPERTY

Commercial property consists of lots and buildings specifically designed for businesses. These properties range from doctors' offices to malls. They all share some common features, however. First, they are not designed as living spaces. People do not reside in commercial properties; they work in them. Second, commercial properties have design features not commonly seen in residential properties — parking lots, elevators, and trade and customer entrances. They must abide by

<sup>1</sup> *Hughes v. Young*, 115 N. C. App. 325, 328, 444 S.E.2d 248, 260 (1994).