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Step 8: Understand Purchase Contracts

Once you have found a house you like, you must negotiate with the seller to buy it. By law, all real estate contracts must be negotiated in writing. Therefore, in order to ask a seller to sell a property, a buyer must submit a written offer. This offer is called a **purchase contract**.

Purchase contracts vary by locale, but they usually contain similar elements. Some are much longer than others. The contract is divided up into different parts or sections each dealing with a particular aspect of the offer. Contracts typically contain the following elements:

Offer to Purchase- A section which lists the purchasers' names, the property address (number, street, city, county), an offer price, and a deposit amount. All purchase contracts should be accompanied by a check representing an **earnest money deposit**. This deposit indicates the buyer's interest in buying the property and, in contract terms, is the **consideration** which generally accompanies an offer of intent to be bound by a contract. Offers will not be considered by a seller without an accompanying deposit. It is applied towards the down payment.

A few thousand dollars is generally sufficient to indicate seriousness. Some agents don't believe the size of the deposit makes a difference and caution against offering large ones. This is reasonable since the deposit goes into an escrow account, and neither the seller nor the buyer have access to it until closing. Other agents believe that a seller will jump at an offer with a large deposit. How much it affects the seller probably depends on the situation and the nature of the offer. In some markets it is custom to submit a deposit representing a certain percentage of the value of the house. In hot markets, such a deposit may influence a seller.

Nonetheless, if you can avoid it, try not to submit a huge deposit check. That deposit is money you don't have the use of from the time you submit it until closing. In addition, if for some reason you lose the deposit, you don't want to lose too much.

Time to Ratify- The buyer generally gives the seller time to review the agreement and document a response. Generally it is 1-2 days, but it varies based upon local custom and market activity. A shorter timeframe is preferred so that both buyers and sellers can plan accordingly. The deadline for response may be included in the document.

Fixtures and Personal Property- This section discusses all the items that you would like included in the purchase price. Fixtures are items that are attached to the property, such as lights, bookcases, carpeting, or shrubbery. Personal property is any item that is not attached to the property, such as appliances, garbage cans, or furniture. Generally, if something is attached to the property, it is assumed to be sold with the property unless otherwise stated by the seller. For your safety, it is in your best interest to clearly indicate what fixtures and personal property you want included. A buyer can never say too little in this section. Most disputes over contract meaning arise from an inadequate identification of the fixtures and personal property included in the purchase price. Err on the side of caution and include everything that is intended to be purchased.



Financing- A section which discusses the buyer's intended method of financing the purchase. Typically it discusses the rate and terms of a conventional mortgage and/or a second mortgage and the amount of the down payment. If the buyer intends to finance the purchase with an FHA or VA loan, this is stated as well. If the buyer intends to assume the existing loan, this would be described in the financing section. If seller financing will be provided, this will be discussed. Any other financing items germane to the purchase are also discussed.

Conventional mortgage financing generally has no impact on the seller unless s/he will be paying points. However, FHA/VA loans may require a seller to transfer the house in good condition, meaning that whatever repairs an FHA/VA inspector requires must be made by the seller before the closing can take place. FHA loans may or may not require some seller involvement in financing as well, such as payment of points or closing costs.

If a buyer has been pre-approved for a loan, it might be helpful to state that in the contract. All other things being equal, a buyer who has already been approved for a loan might be a stronger candidate for purchase than one who has not. A pre-approved buyer might be able to close on a house quicker than one who must obtain financing.

Probably the best offer is an all-cash offer. These are less common, but they do exist. The buyer borrows no money and pays for the home with any funds available. A pre-approved loan is ostensibly an all-cash offer as there is no question that the buyer has the money to purchase the house. If you are making an all-cash offer, the seller should be flattered. Sometimes, however, sellers (or their agents) don't believe the offer when they see it. They may ask for proof that the cash exists. It's your option as to whether or not you want to disclose the source of the money for an all-cash offer.



A seller will judge an offer not only by its purchase price, but also its financing. Typically, everything else being equal, a seller might prefer the offer with the financing vehicle requiring the least seller involvement. An all cash sale is probably most desirable, however, these are rare. A smart seller will speak with the agent or with you to ascertain your true capacity to obtain the financing you listed in your offer. The seller might be willing to accept a slightly smaller offer that is realistic rather than a higher offer that appears more risky.

Escrow- Escrow lists the expected closing date in legal terms, how possession (keys) is to be transferred, and the condition in which the seller must leave the house for the buyer. The day the buyer takes possession is also listed. It may or may not be the same as the closing day.

Title- The title discusses what type of title will vest with the purchaser and how and when it will be transferred. It also might describe the title insurance policy required. There are different types of title a buyer can receive:

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