



NOTICE CONCERNING “NON-RECURRING CLOSING COSTS”

During the course of negotiations, it is often common for the Seller to credit the Buyer in escrow with a certain dollar amount labeled “credit for non-recurring closing costs.” Such closing costs consists of expenses incurred in the transaction customarily paid by the Buyer, such as title insurance premiums, a lender's processing fee, loan points charged by the lender, or a mortgage broker fee. This credit may be given as compensation for physical defects found by the Buyer during the course of inspections, or for other reasons. In entering into such an arrangement, the parties should be aware of the following.

1. **Overvaluing the Property is Prohibited.** Federal law (18 USC §1014) prohibits parties to a sale from willfully overvaluing a property for the purpose of obtaining a higher loan. A violation can occur even if the lender does not rely upon the statement in the loan application or suffer any loss. Bank fraud carries severe penalties and can result in the forfeiture of the property involved.
2. **Credit Must Not Exceed Buyer's Actual Closing Costs.** If the credit for non-recurring closing costs exceeds the amount of such costs incurred by the Buyer as shown on the escrow closing statement, then the Seller is, in effect, making an undisclosed gift to the Buyer of a portion of the down payment or reducing the purchase price. Statements made on the loan application would then be false and would render the transaction illegal.
3. **Limits on the Amount of Permissible Credit.** Regulations promulgated by the secondary mortgage market, such as FannieMae, set limits on the amount of “contributions by interested parties” - another way of referring to payment by the Seller of non-recurring closing costs. If these “contributions” exceed certain limitations, the lender must make a downward adjustment to the property sales price to reflect the amount. Normally, if the property will be used as a principal residence, 3% of the sales price or appraised value is permitted. A percentage of 6% is permitted if the down payment is 20% or more. The limit on investment property is 2%.
4. **Effect on Transferring the Tax Base.** California Revenue & Taxation Code §69.5 allows persons who are 55 and older to transfer the base-year value of their property to a replacement dwelling. One of the conditions is that the “full cash value” of the replacement property is equal or lesser to that of the original property. “Equal or lesser value” means that the fair market value of the replacement property on the date of purchase does not exceed the market value of the original property as of its date of sale, with an adjustment of 5% allowed for each year after the original sale, not to exceed 10%. While ordinarily the “full cash value” is the same as the purchase of sale price, County Assessors have held that “full cash value” does not include non-recurring closing costs. This should be considered in selecting the replacement property.

Receipt of this Notice is acknowledged by Sellers.

Seller _____ Date _____

Seller _____ Date _____

Receipt of this Notice is acknowledged by Buyers.

Buyer _____ Date _____

Buyer _____ Date _____

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