

What is the challenge for real estate purchasing?¹

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ABSTRACT

Nowadays, buying real estate has become a real challenge. Indeed, the contracts become complex and the taxes important. This is why the percentage of profitability drops and young people are less and less attracted by the purchase. This article presents the different aspects concerning the contract and the payment for a property

Key words: Real estate, Purchasing, Investment, Leasing, Property, Warranties

INTRODUCTION

What is better, leasing or purchasing property? It's an eternal debate and for which there is no right or wrong answer, but we are sure about one point: the decision must be part of a life plan. Indeed, everybody requires a place to live; however the concept of owning propriety is becoming increasingly rare. It's an essential and complex question that everyone has to think about, especially for generation Y (people born between 1980 and 2000), young people who are starting to save money.

Does becoming a real estate owner still make Generation Y dream? Generation Y also called, "rental generation" is outdated by the concept of ownership. Why own a car or an apartment at the time of Uber and Airbnb? Concepts more and more present in our life that induces us to have nothing more. More, a Nielsen survey found that 62% of Millennials "prefer to live in dense and diverse urban villages where social interaction is within reach." To be able to afford this lifestyle, Generation Y has no choice but to rent. Other factors can deter the Generation Y from owning a home. They don't want to maintain a home and take responsibility for selling.

Between 2000 and 2010, buying a house was quickly more interesting than renting it. What is the situation today? The answer is not so simple. And if real-estate prices remain globally high, they are trading!

The most important factor is the cost and profitability of the investment. In each case, there are advantages and disadvantages to both options, and the decision requires lots

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of analysis and planning. Both contracts are complicated and determine the up-front cost, monthly recurring cost, taxes, warranties and notices. So we are going to analyze them to see what can be profitable or not and what can be an inconvenient or not.

If you decide to purchase a real estate, you need to establish different contracts for the transaction. The contract determines different terms such as title to the property, earnest money deposit, improvements and fixtures included, purchase price and conditions of payment, real-estate taxes, assessments, and adjustments, special conditions and other statements. When you sign a purchase real-estate contract, you have to initial a lot of pages and sign different pages. What is important in these complex contracts? In this article, different terms will be described in order to explain what is relevant.

Objective statements

The objectives of this paper are to answer to the following questions regarding the payment:

1. What if the transaction cannot be made?
2. How secure the payment?

METHODOLOGY

Step 2 → feasible alternatives solution

1. Identify retraction times and impacts on the cost of the transaction: time for retraction and condition precedent to obtaining a loan
2. Protect your future real estate by making an inventory and indicate who has to pay the different costs (closing costs, house inventory)
3. Build your own contract of purchase of your property with the necessary clauses to secure the payment of the transaction

Step 3 → developments of outcomes

1. Identify retraction times and impacts on the cost of the transaction: time for retraction and condition precedent to obtaining a loan

The purchase of real estate is done mainly through personal contributions but also with the contribution of a bank loan. However when a sales contract is signed there are several deadlines to respect. At the first signature, a period of 7 days is available to retract without any necessary reason. A loan is granted in a longer period of time to

allow the bank to verify the ability to repay the loan if there is a problem and assess the risk of this problem occurring.

This is why in a real estate sales contract there is a condition precedent that allows the future purchaser of real estate to give up the promise of sale if does not obtain the requested mortgage. The promise of sale must indicate that the sale price is paid in whole or in part by a mortgage. If the mortgage is refused, the future buyer can waive the promise of sale without any fees. It must be fully refunded the deposit paid to the seller or the real estate professional. On the other hand, if the suspensive condition is fulfilled, the sale becomes definitive. it is therefore important to insert this clause in order to protect yourself from the purchase if the bank loan is refused.

Then, if you want your offer to buy depends on the sale of your current home must ensure that a period is present in the contract to find a buyer. Deadlines can vary from 30 to 60 days. At the end of this period the transaction cannot take place.

2. Protect your future real estate by making an inventory and indicate who has to pay the different costs (closing costs)

Different points concerning payment are to be taken into account when negotiating a contract for the sale of real estate. The main one, which centralizes all the different fees, is “closing cost”. This is a non-negligible sum that can be paid by the voucher it is necessary that this part be stipulated in the contract. (The closing costs are fees paid at the closing of a real estate transaction). The amount can be indicated in dollars or as a percentage of the purchase price of the house.

3. Build your own contract of purchase of your property with the necessary clauses to secure the payment of the transaction

Building your own contract can be very beneficial. However, this requires having high knowledge in the legal field and a notary must accept the contract.

A real estate transaction is a common fact that most people face at a moment of life. So there are well built templates. There are also people who can take care of this type of contract (real estate agency, notary...).

Step 4 → selection criteria

This article is an analysis and a comparison of this alternative. We can conduct this analysis with 4 attributes:

- Security

- Time
- Price
- Legal feasibility

After this analysis we will be able to choose one (or several) alternative(s) according to the highest score in the comparison (attributes' relevance). Below this is a qualitative analysis of the feasible alternatives.

Multi attribution decision matrix

Attribute	Retraction time	Closing time	Build your own contract
Security	High	High	Low
Time	3 months	Few time	2-3 months
Price	Low	Medium	Good
Legal feasibility	Good	Medium	Low

Fig 1. Multi Attribute Decision Making

According to the MADM, the 2 best opportunities are: **Retraction time and Closing time.**

FINDING

Step 5 → Analysis and comparison of the alternatives

For the analysis we compare these alternatives with quantitative representation. For this, we can choose quantitative number for each relative option.

	Security	Time	Price	Legal Feasibility
High – 3 months – excellent	1	0	0	1
Good	0,75	0,2	0,4	0,6
Medium – 2 months	0,30	0,5	0,75	0,4
Low – Few time	0	1	1	0

Fig 2. Quantitative representation of the attributes

Thank to this quotation we can make the “relative weighting”

Attribute	Retraction time	Closing time	Build your own contract
Security	1	1	0
Time	0	1	0,5
Price	1	0,75	0,6
Legal feasibility	0,6	0,4	0
Total	2,6	3,15	1,1

Fig 3: Relative weighting

With the relative weighting we can see that Retraction time with a total score of **3,15** is 1,2 “better alternative” than Retraction time (3,15/2,6) and 2,8 better alternative” than build your own contract.

It’s a good comparison but we can explore more the alternative with the “**additive weighting technique**” by ranking each attribute by importance.

The ranking for the importance for attribute is:

- 1: Legal feasibility
- 2: Time
- 3: Price
- 4: Security

Attribute	Ranking	Weighting	Retraction time		Closing time		Build your own contract	
Security	4	0.4	1	0.04	1	0,4	0	0
Time	2	0.2	0	0	1	0.2	0,5	0.1
Price	3	0.3	1	0,3	0,75	0,225	0.6	0.18
Legal feasibility	1	0.1	0,6	0.6	0,4	0,4	0	0
Total	10	1	TOT	0.94	TOT	1,225	TOT	0,28

Fig 4. Additive weighting technique

Step 6 → Selection of preferred alternative

Thank to this analysis we can see that closing time is the better alternative than retraction time or build your own contract.

So we can rank the different options in the following order:

- Closing time
- Retraction time
- Build your own contract

So the preferred alternative is **closing time**.

Step 7 → Monitoring post evaluation performance

This analysis was done to find the best option, which will protect the buyer from payment issues. For this we had to determined and make a choice in order to see and choice to best relevant that's why if we take another ranking for the attribute the ranking might change. But the analysis was done thank to research and analysis.

CONCLUSION

In this article we have an analysis for the payment requirement for purchasing real estate contract. In this kind of contract, you need to be careful about several points. The more important topic is the closing cost that is an important part because it defines all the costs (who has to paid) then we have the retraction time as an important part because it helps the buyer to retract if they don't want any more or can't pay. Otherwise, it is useless to write our own contract because mistakes can occur. The generation Y has to continue to purchase some real estate because it's important for the patrimonial.

FOLLOW ON RESEARCH

→ The research can be continued by cost analyzes, so someone with a more "financial" point of view needs to know what is the best solution between buying and renting real estate according to current costs

→ We can use some tools like Google scholar to see if there are any researches that have been done or analyze even more deeply the contract issued and the evolution of the laws.

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About the Author



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Clémence Simon was born in 1995 in Lille. She grew up with her 5 brothers and sisters in a familial house in Lambersart next to Lille and went to the high school nearby. She was a motivated and dynamic child. She practiced gymnastic during 13 years, tennis during 10 years, played the piano and was involved in the “Scout de France”. Clémence is a dynamic and spontaneous girl; her main values are respect, dynamism, family and trust.

She loves being part of projects that’s why in 2012, after high school she went to a school named “Iteem”. Iteem is an engineering school of Centrale Lille co-directed by Skema Business School which trains its students in engineering, but also management and entrepreneurship. During her studies Clémence undertook projects such as a humanitarian project in Cambodia, treasurer of an association that participates in sailing races, member of the student's office...

Clémence likes to travel and discover new cultures. She has had the opportunity to experience many countries but also to live in independence. In 2015, she went on an 8-month internship in Singapore working with a Luxury Cosmetics SME.

Today, Clémence is in the 5th year of study during which she mixes her master's degree in engineering at Centrale Lille with a Master of Project and Program Management and Business Development at Skema Business School. During school, she also had the opportunity to do in total 15 months of internship. That’s why she had a business culture and knows about the world of business. This last year is a real challenge because in addition to being a complete year, it will culminate in the launch of her professional career. If you want to know more about Clémence Simon, you can contact her at clemence.simon@skema.edu