



SHEEHY TEAM

INVESTMENT GLOSSARY



Addendum - Any additions that accompany a purchase contract, amendments need to be agreed upon to be valid.

Aerial View – A picture of a property from the air, whether by airplane or by satellite that tells: 1) saves a lot of time looking at a property in person and shows the neighborhood, 2) verifies the state of the property from angle you can't see driving by. This is especially crucial for out of town buyers.

Amortization Schedule – A financing re-payment schedule that shows you your principle balance paid, interest paid, and shows how long and at what cost you are to pay off your debt.

Appraisal – sometimes used interchangeably with an assessment - a bank ordered document (in most cases) that is third-party that tries to put value on the property. Done by a professional and licensed Appraiser, the bank wants to know can the property cover the loan. Based on three approaches income approach, replacement approach

Assignee – The process disclosed in the contract and agreed upon by the seller, in which the buyer's representative may hide the buyer's identity-who would assume the property at closing. Usually this is done in the case of a corporation which isn't actually an individual.

Capital Gains Rates (or Capital Gains) – the profit you get above the selling price. The Capital gain has nothing to do with financing. You must also factor in depreciation and non-expensable improvements.

Capital Improvements – Structural improvements or restoration that will either enhance the property's overall value, appearance, or increases functionality.

Capitalization Rate - or Cap Rate – Answers a simple question: what is the effective interest rate that this investment yields? It is a percentage which gives you an estimate of the effective return on the entire purchase price that a property can generate.

Cash Flow – the amount of cash that you have left over each month for a given property after all rent is collected, all pro-rations are set aside, all expenses are paid, and the mortgage on the property is paid.

Cash on Cash Return – a calculated number found by dividing the annual cash flow by the amount of cash that was necessary to secure the financing for the property. Different than a Cap Rate, this number varies based upon the amount of cash necessary to secure the financing for purchase.

Closing Costs - HUD or Settlement Statement - an accounting sheet that concludes a purchase contract. When writing a contract to purchase property...the HUD includes, the purchase price, costs of due diligence, and all closing costs -- including lender fees, inspections, surveys, title work, and any repairs or contract amendments of any costs will be on this document. This document determines who pays what to close the real estate transaction.

Collateral - Any real or personal property having marketable value that a borrower pledges as security in order to obtain a loan. In mortgage transactions, specific land is the collateral.

Commercial Property - property that is generally used for investment purposes (examples are a freestanding building, commercially-zoned land, apartment complex, strip center). Generally refers to any real property except a 1 to 4 unit single resident.

Commission – Compensation provided to a service representative for the legal advocacy and administration work done on behalf of the client. Usually expressed as a percentage. In real estate, an agent would be paid at the sale (or close) of a transaction through the closing agency.

Comparable Market Analysis - (commonly referred to as COMPS) an approach to assessing the value of a property in that the focus is on the market value of property based on the sale of other comparable homes of similar value and/or in the neighborhood.

Corporation – a legal entity with its own tax identity similar to an individual's, which can represent interest in investing. A corporation exists to provide some insulation from liability.

Debt Service – The amount of the monthly payment on a mortgage. The loan originator usually charges regularly recurring fees that are charged for the use of the borrowed funds – called interest. The original amount borrowed and its remaining balance is known as the principal.

Deed – a legal document that conveys the title (or ownership) of the property.

Default – a breach in the terms of the contract. There can be pre-negotiated penalties or there may not be any loss. A law suit could also take place if there is a loss due to the assumption of the sale of property.

Deferred Maintenance – Lot of undone work on the property (broken windows, cracked bricks, painting, roof in disrepair).

Depreciation – a tax law benefit associated with property ownership that that allows you to assume that every year your property is worth less. About 2.5% annually, depreciation reduces your taxable income. A way offset income, you can take it as an expense as a matter of speaking. You can recapture this when you sell.

Disclosure - A legal requirement by which the sellers of specific types of property or under certain circumstances must reveal whether there is a knowledge of specified information to potential buyers (such as lead-based paint, mold, asbestos, or other potentially hazardous substances).

Distressed Property – is concerned with financing, not the actual property. In theory, if the bank is willing to work with an investor, can be a really good deal. Be careful, the banks owe more than the property is worth, so do a good analysis and make sure it's a good deal regardless of whether it's distressed or not.

Due Diligence –See Option Period

Earnest Money - A sum of money (usually about \$500) offered by a prospective buyer as a sign of good faith in with an offer to purchase a property from the seller. This money is surrendered unless the seller agrees to release it or in the case of a lack of agreement.

Effective Gross Income – Income of the property before debt service. Income from all rents collected minus expenses (such as lawn service, property taxes, insurance, vacancies, utilities, all expenses,

Equity – The difference between what you owe on a property and what is its net value. Theoretically, it's the effective value of a property after its sold debts paid off.

Escrow - An account arrangement by a lender (rather than bank or owner finance) into which the borrower pays for taxes and insurance.

Estoppel Certificates - A document signed by the tenant disclosing the current conditions of the lease and any additional agreements between the landlord and tenant.

Eviction – The legal process of removing a tenant from the property for defaulting on the lease in some way, usually for lack of rent payment. The judge will rule. The Sheriff can help escort the tenant off the premises.

Fair Housing Act - The Fair Housing Act establishes a national policy of fair housing. The law makes it illegal for any person or business to discriminate in the sale, lease, advertising, or financing of housing or making housing otherwise unavailable because of: race color religion sex, handicap (disability), or familial status national origin.

FHA – Federal Housing Administration – guarantees a loan for lender (or bank). Usually refers to federal mortgage insurance for lenders to finance borrowers who are usually lower-income and have difficulty coming up with a down payment, which is a requirement of a typical mortgage. The catch here is that the money would be paid back through insurance premiums. Originated in the 1930s amidst massive foreclosures.

Financing – how you will pay for a purchase. This amount of money is borrowed. Answers the question in a real estate transaction of how much of the purchase will be cash and how much will be borrowed. This amount is to be eventually paid back with interest and is shown on an amortization schedule, Examples include: FHA, VA, Conventional.

Foreclosure – releases the property of primary and secondary liens on a property. Various counties have different policies associated with foreclosure. The bank reassuming the property and a default on a loan may auction the property starting the bidding at the cost they are trying to recoup from the property. After foreclosure only tax, federal, and state liens remain.

Gross Rent Multiplier – is calculated by taking the purchase price of the property and dividing it by the gross annual rent. This number gives you an idea if the gross rent on a property is sufficient enough to justify the purchase price on the property. A low gross multiplier number is desired and ideally it will be below 3.

Gross Rental Income – the maximum potential rent possible for a given property at the current rental rates assuming that all units are rented and all tenants pay.

Income Approach - an approach to analyzing the value of a property (aka valuation) in that the focus is on the income. This number is calculated by taking the NOI and dividing it by the CAP rate.

Income Statement – AKA Profit & Loss statement (or P & L) – All Income and Expenses demonstrating how a property is performing in a given period of time. It shows in theory the income potential of a property under the circumstances of the current owner.

Inspection Report – The goal is to feel comfortable that you understand the typical condition of the property. Seek out a licensed inspector to check all vacant units and a sufficient number of occupied units. Report should have an estimate of deferred maintenance. See Appraisal

Interest or interest rate - The loan originator usually charges regularly occurring fees that are charged for the use of the borrowed funds. These fees are usually expressed as a percentage of the principal loan amount. The loan rate is based on the credit risk of the borrower and the inflation rate.

Intermediary Status – a condition in real estate when both sides of a real estate transaction (both the buyer's representative and the seller's representative) take place under the same broker. This must be disclosed on the contract and takes place either when one agent represents both buyers and sellers or when two agents under the same broker represent's one or the other.

Lease – A contract agreement between a tenant and a landlord that spells out the terms of tenancy. The lease explains: how long the tenant, who and what can live in the property, the use of the property, and who pays for what (such as utilities, taxes, rent, and insurance).

Lease option - usually refers to commercial leases where at the end of a rental lease...there is an option for the leasee (or tenant) to give notice to the owner of their intention to renew the lease for a pre-determined amount (usually at an increase in rate). Essentially this is an opportunity to tenants who have committed themselves to the space they rent to recommit.

Leasing Agent – a person working on behalf of the seller to lease the property. Similar to a real estate agent, except this person is looking only to lease out the unit. A job often performed by property managers.

Leverage – is used when you purchase a property with a little money down. The goal is to get a multiple return on your investment. An ideal leverage to return rate would be 5:1. Two things to be concerned about are debt service and depreciation.

Lien – the assignment of a debt or a notification that there is a debt against an asset. A banker's or mechanic's lien will notify potential purchasers or investors that a debt exists on the property that must be satisfied. A lien effectively holds up title.

LIHTC (or Low Income Housing Tax Credits) – Federal tax credits available through the Tax Reform Act of 1986 that increases affordable housing in a troubled economic market.

They are a mixed bag, due to the limitations and restrictions that accompany these credits.

Line of Credit – money available to you to help you maintain your business. There are two types: secured and unsecured. Unsecured carries with it a higher interest rate than a secured line of credit.

Liquidity – The sale value of real property as represented by real estate market conditions.

Listing Price – The price a seller initially suggests the property should sell for in the market. The price usually reflects market value and the seller's interest in the property. Whether this price is high or low is determined by good analysis of the market and an assessment of the property's performance.

Loan Approval – when a bank approves a purchase and exacts certain requirements on the borrower such as term length, loan amount limit, interest rate and provides a guarantee that they will finance the purchase at closing.

Loan Origination Fee - A fee charged to the borrower by the lender for the administrative costs of processing and creating a mortgage loan which is usually computed as a percentage of the loan amount and is often expressed in points.

Low-Ball Offer - An offer from a prospective property buyer that is much lower than the listing price which may indicate that the buyer believes that the property will not receive many good offers and that the buyer is interested in the property only if it can be purchased at a bargain price.

Market Analysis – when you look at the market and interview what other people are renting or selling. For rentals: figure out what units in a similar area and similar unit type are renting their units. For sale: get a slice of approximately 5 units that are on the market, 5 units that have recently sold and figure out where your property fits and at what price you could sell it.

Market Rent – the typical rent you could expect to find for a particular unit in a given area. The market rent helps determine what your rents would be. You really can't deviate too far from the market unless your apartment has a compelling case.

Market Rent Analysis – current market rents for comparable units in the market that you are considering for purchase

Market Survey – This is a helpful tool which gives provides direction to what rate to set rents at. The rental amount needs to be close to what rates are set at for comparable rooms in the area. This tool can sometimes be found at the local chapter of the Apartment Association

Meets & Bounds – a linear description of the boundary line. Theoretically, with this document you could walk the perimeter of the property.

Month-to-month tenancy - at the conclusion of the lease period this is a default state of leasing whereby the major facets of the lease remain binding on landlord and tenant with the exception that it's a month by month agreement. In which case only a 30-day notice would be required to vacate the property.

Mortgage – A loan to finance the purchase of real estate. Comes with a payment period and interest rates. The borrower (mortgagor) gives the lender (mortgagee) a lien on the property as collateral for the loan.

Net Income Multiplier - or NIM - a helpful number is analysis to estimate the value of rental property. A useful way to see how the property is performing relative to its market price. This factor when multiplied by the Net Operating Income or NOI gives you a estimate of the property's value.

Net Operating Income – or NOI – is the difference between the total rent collected minus all expenses. This number doesn't count debt service, which is factor that would change based on the owner's credit and personal finances.

Operating Expenses – Whatever costs incurred while attempting to maintain and run a business. The include lawn service, property taxes, insurance, vacancies, utilities,

Option Money - or Option Fee – an amount usually about \$100 or more...which is a “get out of jail free” card. A small loss that helps you make sure you're offer price is adequate and whether or not, any changes to contract are needed to accomplish a fair closing.

Option Period – or Due Diligence – the period of time written into the contract a buyer has the opportunity to inspect a property including but not limited to the financials, insurance, tax records, mortgage copy, leases, rent rolls, estoppels certificates, etc.

Portfolio – a summary of all investments and some information about their performance.

Prime Rate (or prime) - The lowest rate interest that a lender or mortgagee, such as a bank would charges its most credit worthy customers. This rate is set by the Federal Reserve; it's the rate for banks to borrow from each other and from the Federal Reserve.

Principal – a word with many uses in real estate...for investors it refers to an amount invested which is different than income or profits.

Private Mortgage Insurance – (PMI) – aka mortgage insurance. It is distinguished from FHA and VA insurance, which are government-run programs. The cost of insurance varies depending on the size of the down payment and the loan amount; it's typically only about one-half of 1 percent of the loan. The borrower pays the premiums, but the lender is the beneficiary. The coverage protects lenders against the borrower's default. If your down payment on a home is less than 20 percent of the appraised value or sale price, you must obtain mortgage insurance.

Profit & Loss - (P & L) – This will show you the expenses that you will inherit with the purchase of the property. Like gas, electricity, water, trash, sewage, and insurance. Being able to see the expenses going back 2 or more years is preferred to understand a properties performance.

Promissory Note - (or note) the mortgage. The money borrowed or financing incurred for the purchase of a property usually paid monthly with a principal and interest component.

Property Tax – Annual payments to the county, city, schools, colleges, etc that are assessed upon property owners.

Property Tax Records – a free and useful tool for determining the value of a property that is maintained by the Tax Assessor. Allows you to do your own analysis on a property. This tool provides important information such as the year built, history of property, sq footage of improvements and land, address and name of owner or corporation, & deed date.

Quit Claim Deed – A deed transferring whatever interest in a property or title, without warranty.

Real Estate Leverage – see leverage

Refinance (or Refi) – An investment decision whereby additional moneys are borrowed to pay off an existing loan. It's usually the same loan amount and uses the same property as collateral. In most cases, this is done to switch financing from adjustable rate to a fixed rate mortgage

Rent Roll – a generic document that shows the vacancy rate on a property. Usually you will see tenant name, rent amount, move-in date, lease dates, deposit, and unit information such as the number of 1, 2, or 3+ units. Compare the rent roll to the leases verify that they match up exactly.

Rental Income – the income that you generate from collecting rent.

Replacement Cost - an approach to assessing the value of a property in that the focus is on the cost of it would take to build the existing property today, minus a depreciation schedule based on how many years it's been in place.

Return on Investment – or ROI – similar to cash on cash return

Sales Price – aka the purchase price – is the agreed upon amount of money needed to purchase a given property between the buyer and seller. This amount is usually negotiated through a realtor to be mutually beneficial if possible.

SBA – (Small Business Administration) - Federal agency that assists small businesses with advice, financing, and other business development aid. The SBA itself does not make loans, but guarantees repayment of loans made by a bank or finance company.

Security deposit - money received from the tenant that is paid when a lease is executed with the lease (or tenant). This money insures that tenant will perform the responsibilities of the lease; it's a way to hold the tenant accountable for the stewardship of the property.

Settlement Statement – see Closing Statement

Special Purpose Properties - properties that meet special community purposes such as mini-storage facilities and mobile parks.

Survey – an aerial diagram showing boundary locations and measurements of the buildings on property. Easements, flood plains, number of lots, and lot size for a given property. Must be obtained from a licensed surveyor.

Tax Assessment – An appraiser is someone who appraises all the properties in a given county each year. Some fight to keep their assessors to keep property assessments low. Nowadays assessments can be higher, investors need to do their analysis and not see this amount as a purchase price.

Tax Certificates - A certificate prepared by the mortgage provider or investor indicating whether property taxes and special assessments on mortgaged property have been paid.

Title –This document usually prepared and insured by a title company reveals any financial problems. A clear title is expected at a closing. The title company will research the previous and current owners of a property to see if there are any liens or anything that should be disclosed about the true value of a property.

Title Commitment - A promise to issue an insurance policy on a piece of property. Organized into five main parts it tells 1) Who is being insured, 2) the amount of the insurance — the sales price, 3) what is insured--the legal description of the property 4) What is required to insure the title -- no liens and a signed affidavit, 5) what is not insured. The purpose is to insure a clean title for purchaser, seller, and a lender of the sale of the property. It fully discloses whether certain requirements have been met or whether there are any burdens, liens especially that will prevent a lender from being in first-position in the case of a default on the loan.

Title Insurance –The title researches current and past owners of a given property for sale looking for liens on the property. Banks desire insurance for their loans. If the title is clear, this puts the lender in first position, which excludes anyone else from being compensated instead of the bank to reclaim their lost.

Triple Net Lease – An agreement where the tenant is going to pay property taxes, insurance, and all maintenance. The advantage to the seller is that it's like you sold it, but you still own it...there wouldn't be any expenses. Usually used in commercial real estate transactions.

Unit Matrix – all units on the property with room count, square footage, and current rent, etc.

VA – Veteran Affairs Loans – A loan guaranteed by the US Department of Veteran Affairs. VA loan can now be used to buy a home with no down payment. The Department of VA recently increased the Maximum Guaranty Amount for veteran home loans to as much as \$729,750. However, VA and FHA have non-allowable fees that are usually charged to the borrower; often these are charged anyway, but to the seller. This can effect contract negotiations.

Vacancy Rate/Factor – The percentage amount of vacant units to occupied units. In my analysis, I count vacancies as an expense, which provides a clearer picture of performance because vacant units aren't collected income and do incur expenses, such as insurance and

Warranty Deed – A deed which guarantees the title for a property from the seller to the buyer.



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