

Trump University Real Estate Glossary

“A regular part of your day should be devoted to expanding your horizons”

– Donald Trump

Glossary of Real Estate Terms

Adjustable rate mortgage (ARM)

A mortgage loan that typically has a fixed initial interest rate and after that period, the interest is adjusted to reflect market rates and terms of the loan. For example: a person obtains a 5/10 adjustable-rate mortgage to finance the purchase of a home. The interest rate is fixed for first 5 years then changes to become adjustable for the remainder of the term of the loan and the interest rate floats to reflect market conditions.

Appreciation/growth

An increase in the value of a property. Causes for appreciation for real estate may include inflation, demand pressures for land and buildings or a physical addition or improvements.

Example: John sold land for \$150,000 that he purchased 12 years ago for \$95,000. During that time the amount of appreciation was \$55,000.

Note: Appreciation gains from investment property are generally subject to capital gains taxes, rates vary depending on the circumstances.

Capital gain

A financial gain on the sale of a capital asset.

Example: Judy purchases land, for investment purposes, for \$100,000. Some 13 months later she sells it for \$140,000. She reports the \$40,000 profit as a capital gain on her income tax return.

Capitalization rate/Cap rate

A rate of return used to derive the capital value of an income stream. The formula is

$$\text{Cap Rate} = \frac{\text{Net Operating Income}}{\text{Sales Price}}$$

Cash flow

The amount available after deducting all periodic cash payments, expenses and debt service from rental and other income. Cash flow can be either negative or positive.

Cash-on-cash return/yield

Equals annual cash flow, or amount available after all expenses and debt have been paid, divided by the deposit or down payment amount, expressed as a percentage.

Comparative market analysis (CMA)

An estimate of the value of a property using indicators taken from sales of comparable properties, typically in the same area with similar properties - number of bedrooms, bathrooms, similar age, similar square footage or meters. They can be compared on price per square foot. These value estimates are not appraisals.

Compounding interest

Interest paid on the original principal and also on the unpaid interest that has accumulated.

Example: \$100 deposited in a 5% savings account earns \$5 interest the first year. Its second-year earnings are 5% of \$105, or \$5.25. Each year, interest is received on previously earned but undistributed interest, so interest compounds.

Exchanging into properties

Under section 1031 of the Internal Revenue Code, this is a tax-deferred exchange where tax on profits from sale of one property are "deferred" because they are used in the purchase of a "like-kind" property. There are strict guidelines under which this must occur with timing limitations and requirements for the handling of funds.

FICO (Fair Isaac Company) score

A measure of borrower credit risk commonly used by mortgage underwriters when originating loans on owner-occupied homes. The score is based on the applicants' credit history and the frequency with which they use credit. Expressed as a number between 300 and 850, the score determines not only whether the loan is approved but also what type of terms the lender is willing to offer, based on the risk of you as a borrower.

Flippers/flipping

Purchase and resale of property at a quick profit.

Floating interest rate

An interest rate that is not fixed over the term of a loan, bond, or other fixed-income security, but is allowed to vary according to the change in a specified index.

Gresham's Law – stated as

"Bad money drives good money out of circulation."

Leverage

Use of borrowed funds to increase purchasing power and, ideally, to increase the profitability of an investment.

Liquidity

Ease of converting assets to cash.

Example: common stocks and U.S. savings bonds have good liquidity. Real estate and many types of collectibles generally have poor liquidity.

Mortgage – adjustable rate

See adjustable rate mortgage (ARM)

Mortgage – fixed rate

A loan secured by real property featuring an interest rate that is constant for the term of the loan. Contrast with adjustable rate mortgage.

Rent

A charge for the use of space.

Rental income

Actual amounts collected from tenants for the use of space; does not include miscellaneous income, e.g. laundry income or special fees. To avoid confusion, it is preferable to qualify rental income as actual, potential, or effective.

Triple net lease

One in which the tenant is to pay all operating expenses of the property; the landlord receives a net rent.

Example: Big Buy Supermarkets enters into a triple-net lease. They are to pay for all the taxes, utilities, insurance, repairs, janitorial services and license fees; any debt service and the landlord's income taxes are the responsibility of the landlord.

Upside-down investments

Investments that are not paying out a return, but are costing money to hold.

Vacancy rate

The percentage of all units or space that is unoccupied or not rented. On a pro-forma income statement a projected vacancy rate is used to estimate the vacancy allowance, which is deducted from potential gross income to derive effective gross income.

Velocity of money

The rate at which money invested will be returned to you - how quickly can you have the money back in your hands to use for another deal.