The ABCs of Real Estate

Acre: A parcel of land that measures 43,560 square feet.

Ad Valorem Taxes: Property taxes on the assessed value of property.

Adjustable Rate Mortgage (ARM): A mortgage in which the interest rate is adjusted periodically according to a pre-selector index. The terms, adjustment schedule, and index to be used can be negotiated by the borrower and lender. Specific types include the renegotiable rate mortgage and the variable rate mortgage. Also referred to as a Canadian rollover mortgage.

All-Inclusive Trust Deed (AITD): An alternative to refinancing the entire loan when a borrower needs additional funds, this technique involves the creation of a subordinate mortgage that includes the balance due on the existing mortgage(s) plus the amount of the new secondary or junior lien.

Annual Percentage Rate (APR): The percentage relationship of the total finance charge to the amount of the loan. The Term is used in the Truth in Lending Act.

Apportionment: A pro-rate division and distribution of prepaid or accrued taxes, prepaid insurance premiums, prepaid rents and other income and expenses. Apportionment usually occurs when a property is sold, and is the manner of determining the amounts due to or from each party.

Appurtenance: Any tangible or intangible item attached to the land and thus part of the property, such as a building (tangible) or an easement (intangible).

Assemblage: The process of acquiring adjacent parcels of land in order to combine them into a single site for development.

Assessor: A public official who evaluates property for the purpose of taxation.

Assignee: The person of corporation to whom an agreement or contract is assigned. One to whom real property, or an interest in real property, is transferred to set over.

Assignment of Rents: An agreement between the property owner and mortgagee that transfers to the mortgagee the right to collect rents from tenants in the event of a default by the owner.

Assumption Fee: The fee paid to a lender (usually by the purchaser of real property) resulting from the assumption of a mortgage.

Assumption of Mortgage: Assumption by a purchaser of the primary liability for payment of an existing mortgage or deed of trust. The seller remains secondarily liable unless specifically released by the lender.

Avulsion: The sudden tearing away of land by the violent action of a river or other body of water.

Balloon Mortgage: A mortgage with periodic installments of principal and interest that do not fully amortize the loan. The balance of the mortgage is due in a lump sum at a specified date in the future, usually at the end of the term.

Basis Point: This term describes the amount of change in yield in many debt instruments, including mortgages. It is equal to one one-hundreth of one percent.

Blanket Mortgage/Blanket Trust Deed: A mortgage on more than one parcel or unit of land. Blanket mortgages frequently are incurred by subdividers or developers who have purchased a single tract of land for the purpose of dividing it into smaller parcels for sale or development.

Book Value: The capitalized cost of an asset, less depreciation taken for accounting purposes, based on the method used for the computing of depreciation over the useful life of the asset.

Call: An option to buy a specific security at a specified price within a designated period of time.

Capital Expenditure: The cost of an improvement made to extend the useful life of a physical asset, such as property, or to add to its value.

Capital Improvement: Any permanent improvement to real property that adds to its value and useful life.

Capitalization Rate (Cap Rate): Used to determine capitalized value, this rate is the percentage rate of return an investor can expect. It is the net operating income of the property divided by the sales price or value of the property expressed as a percentage.

Cash on Cash Return: The rate of return on an investment measured by the cash returned to the investor based on the investor's cash investment without regard to income tax savings or the use of borrowed funds. It equals the annual dollar income divided by the total dollar investment, expressed as a percentage.

Certificate of Occupancy: Written authorization given by a local municipality to a builder or renovator that allows a newly completed or substantially completed structure to be occupied.

Certificate of Title: A written statement of opinion furnished by an abstract or title company or an attorney after a search of the public land and tax records stating that the title to a piece of property is legally vested in the present owner.

Chattel Mortgage: An agreement between a secured party and a debtor creating a security interest in personal property.

Conventional Mortgage-Backed Securities (CMBS): Securities whose underlying pool of mortgages have no federal guarantees or insurance.

Commitment: An agreement, often in writing, between a lender and a borrower to loan money at a future date subject to compliance with stated conditions.

Commitment Fee: Any fee paid by a potential borrower to a potential lender for the lender's promise to lend money at a specified date in the future. The lender may or may not expect to fund the commitment/

Compensating Balance: A demand deposit usually required by a commercial bank as a condition for extending a line of credit or a loan.

Completion Bond: A bond furnished by a mortgagor to guarantee completion of construction.

Coupon Rate: The annual interest rate of debt instrument expressed as a percentage of its face value, or principal.

Covenant: A legally enforceable promise or restriction. For example, in a mortgage, the borrower may covenant to keep the property in good repair and adequately insured against fire and other casualties. A buyer who breaches such a covenant may be subject to foreclosure.

Debt Coverage Ratio: The ratio of effective annual net income to annual debt service. This ratio often is used as a criterion for underwriting income property mortgage loans.

Deed in Lieu (of foreclosure): A deed given by a mortgagor to a mortgagee to satisfy a debt and avoid foreclosure.

Defeasance Clause: The clause in a mortgage that gives the mortgagor the right to redeem property upon the payment to the mortgagee of the obligation due.

Density: The ratio between the total land area and the number of residential or commercial structures to be placed upon it. Density usually is regulated by local ordinances.

Discounted Cash Flow (DCF): The method of applying an appropriate discount to cash to be received in the future to arrive at the present value of those future earnings. The discount rate used, generally the appropriate cost of capital, incorporates the risk level of future cash flows.

Easement: A right granted to another person to use your land for a specific purpose. Most commonly, easements are granted to public utility and telephone companies for the purpose of running lines on or under the property or to neighbors for the purpose of using a common driveway.

Eminent Domain: The right of government bodies, public utilities, and public service corporations to take private property for public use on payment of its fair market value. This may occur, for example, if a state or locality wants to widen a highway.

Encumbrance: Anything that affects or limits the fee simple title to property, such as mortgages, leases, easements, or restrictions.

Escalator Clause: A provision in a lease whereby real estate tax increases imposed on the lessor are passed along to the lessee as additional rent.

Estoppel Certificate: A written statement setting forth certain facts about a piece of real estate, such as the precise amount of indebtedness remaining.

Exculpatory Cause: A clause in contract holding one party harmless in the event of some default. In a lease, the exculpatory clause relieves the landlord of liability for the personal injury to tenants or damage to tenants' property. In a mortgage, it allows the borrower to surrender the property to the lender without personal liability for the loan.

Flip-flop: A technique in partnership agreements for allocating disproportionately high profits and loss from a project to the cash investors until a certain point in time, then switching (in a "flip-flop") to a different allocation more favorable to the developer. Example: The investors have a 90 percent interest and the developer has 10 percent interest in profit and losses for the first 20 years, after which they shared 50-50.

Floor Area Ratio (FAR): The ratio of the total floor area of a building to the total area of the site. Also referred to as Floor Space Index.

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Forbearance: The act of refraining from taking legal action despite the fact that the mortgage is in arrears. It is usually granted only when a mortgagor makes a satisfactory arrangement by which the arrears will be paid at a future date.

Graduated Lease: A lease in which the rent is fixed for the initial term and increases at certain set intervals by predetermined amounts or by amounts based on periodic appraisals.

Gross Income Multiplier: A tool used to assess the approximate value of a rental property by comparing its rental income with other like properties. It gives the relationship between the gross rental income and sales price.

Gross Rent Multiplier (GRM): A tool used to assess the approximate value of a rental property by comparing its rental income with other like properties. It gives the relationship between the gross rental income and sales price. Also referred to as gross income multiplier.

Guillotine Clause: A clause in a mortgage that enables a lender to call a loan if specified goals are not met.

Holdover Tenant: A tenant who remains in possession of leased property after the expiration of the lease term.

Impound: That portion of a mortgagor's monthly payments held by the lender or servicer to pay for taxes, hazard insurance, mortgage insurance, lease payments, and other items as they become due. Known as impounds or reserves in some states.

Internal Rate of Return (IRR): A method of determining the annualized effective compounded return rate on an investment over time assuming a set of income, expense, and property value conditions as well as risk. It combines the present worth of the right to receive future income streams with the present worth of the right to receive a particular profit when the property is sold.

Kick-Out Clause
- Lease: A clause in the lease that permits a tenant to cancel a lease if the landlord fails to comply with stated conditions or standards.
- Purchase: A clause that protects the buyer by providing that upon the occurrence of some triggering event prior to the deal closing (e.g., seller's acceptance of a new offer) that the buyer has a specific period of time to act (e.g., by matching the terms of the new offer) to avoid being "kicked out" of the contract. The clause must specify precisely what the seller must do to invoke its rights under it.

Life Estate: An estate whose life is limited to the life of an individual. Upon that person's death, the property passes to a beneficiary, who retains the use and possession of the property, but may not sell it. The estate is terminated upon death of the beneficiary.

Loan to Value Ratio (LTV): The relationship of a mortgage to the appraised value of a security as calculated by dividing the loan balance of a property by its market value. This ratio is expressed to a potential purchaser of property in terms of the percentage a lending institution is willing to finance.

Lock-in Period: There are two common definitions for this term:
- The portion of the term of a mortgage load during which the loan cannot be prepaid.
- A set period of time, generally 60-90 days, during which a mortgagor agrees to hold the mortgage rate and points payable by the borrower to the rate quoted when the application was taken.

Mechanics Lien: A legal claim securing priority of payment for work contracted for a performed and material furnished by a mechanic or other person for the construction or repair of a building. The lien attaches to the land as well as any buildings and improvements. The landowner does not own clear title until the debt is paid.

Minimum Lot Zoning: A type of zoning that regulates the smallest lot size permitted per building.

Net Book Value: The capitalized cost of an asset, less depreciation taken for accounting purposes, based on the method used for the computing of depreciation over the useful life of the asset.

Net Present Value: The method of applying an appropriate discount to cash to be received in the future to arrive at the present value of those future earnings.

Non-disturbance Agreement: An agreement that permits a tenant under a lease to remain in possession of the property for the term of the lease despite any foreclosure proceedings.

Non-recourse Loan: A type of mortgage loan in which the borrower cannot be held personally liable in the event of foreclosure.

Opportunity Cost: The amount of return from a real property investment that is distributed entirely to preferred investors until these investors have received a specified return on their investment.

Origination Fee: The fee charged by a lender to prepare loan documents, make credit checks, inspect and sometimes appraise a property being considered for a new loan, Usually, it is computed as a percentage of the face value of the loan. The amount varies according to various factors, including whether the loan is being placed in the prime or subprime market.

Overall Capitalization Rate: A market-derived capitalization rate based on the sale prices and rental rates at comparable properties. The rate is calculated by dividing the net operating income of sale properties by their sale prices.

Overall Rate of Return: A market-derived capitalization rate based on the sale prices and rental rates at comparable properties. The rate is calculated by dividing the net operating income over sale properties by their sale prices.

Plat: A map, drawn to scale, showing the divisions of a piece of land, including streets, boundaries and easements.

Population Density: The ratio between the total land area and the number of residential or commercial structures to be placed upon it. Density usually is regulated by local ordinances.

Preferred Return: Sometimes referred to as “opportunity cost,” preferred return is the amount of return from a real property investment that is distributed entirely to preferred investors until these investors have received a specified return on their investment.

Put: An option to sell a specific security at a specified price within a designated period.

Recourse Note: A debt instrument under which the lender can take action against the borrower or endorser personally, in addition to foreclosure.

Release Price: The amount of compensation needed for a lien to be removed by a mortgagee. The amount may be the full amount of the loan or some part thereof.

Restrictive Covenant: A legal obligation imposed in a deed by the seller upon the buyer of real estate to do or not to do something (for example, not to build on certain parts of the property). Frequently, such restrictions are enforceable on subsequent buyers of the property.

Rule of 78s: A method of allocating interest charges for the life of a loan to the periods within the loan. It is often used by lenders (usually on installment loans) for calculating an interest rebate on a loan paid off, or refinanced, prior to its maturity date or for accruing earned discount.

Sale Leaseback: A technique in which a property owner sells property to a buyer and then immediately leases the property back from that buyer, usually on a long-term basis.

Sandwich Lease: Leasing arrangement under which the lessee becomes a lessor by subletting the property. Typically, the owner of the sandwich lease is neither the owner nor the user of the property.

Setback Lines: Lines that establish required distances for the location of a structure in relation to the perimeter of the property. They are defined in building codes, deed restrictions, and zoning requirements.

Sky Lease: A lease of air rights.

Step-down Lease: A lease that provides for specified decreases in rent at set intervals.

Step-up Lease: A lease in which the rent is fixed for the initially term and increases at certain set intervals by predetermined amounts or by amounts based on periodic appraisals. Such leases are also called graduated leases.

Stop Clause: A provision in a lease whereby real estate tax increases imposed on the lessor are passed along to the lessee as additional rent; also referred to as an Escalator clause.

Subordination: establishment of priority between different existing interests, claims, liens and encumbrances on the same parcel of land, as acknowledged in a written recorded document. Subordination may apply to mortgages, leases, real estate rights, and any other types of debt instruments.

Subrogation: A legal technique under which one person substitutes for another in reference to a debt, claim or right.

Tax Stop Clause: A provision in a lease whereby real estate tax increases imposed on the lessor are passed along to the lessee as additional rent; also referred to as an Escalator clause.

Tenancy in Common (TIC): In the law, the type of ownership created when real or personal property is granted to two or more persons, each of whom has an undivided interest in the property and an equal right to use the property without expressed words creating a joint tenancy. There is no right of survivorship.

Underwriting: The analysis or risk and the matching of it to an appropriate rate and term.

Usury: The practice of taking or contracting for an exorbitant or illegally high rate for a loan. Maximum interest rates are set by state law.

Wraparound Mortgage: An alternative to refinancing the entire loan when a borrower needs additional funds, this technique involves the creation of a subordinate mortgage that includes the balance due on the existing mortgage(s) plus the amount on the new secondary or junior line. Also called an All-Inclusive Trust Deed (AITD).