

Glossary of Real Estate Terms

Adjustable-Rate Mortgage (ARM)

An **Adjustable-Rate Mortgage (ARM)** is a type of loan whose prevailing interest rate is tied to an economic index (like one-year Treasury Bills), which fluctuates with the market. The three most popular types of ARMs are one-year ARMs, which adjust every year, three-year ARMs, which adjust every three years, and five-year ARMs, which adjust every five years. When the loan adjusts, the lender tacks a margin onto the economic index rate to come up with your loan's new rate. ARMs are considered riskier than fixed-rate mortgages, but their starting interest rates are generally lower than a longer-term rate, and in the past five to ten years, people have done very well with them..

Amortization

Amortization is a payment plan which enables the borrower to repay his debt gradually through monthly payments of principal and interest. Amortization tables allow you to see exactly how much you would pay each month in interest and how much you repay in principal, depending on the amount of money borrowed at a specific interest rate.

Annual Percentage Rate (APR)

The **Annual Percentage Rate (APR)** is the total cost of a loan, expressed as a percentage rate of interest, which includes not only the loan's interest rate, but factors in all the costs associated with making that loan, including closing costs and fees. The costs are then amortized over the life of the loan. Banks are required by the federal Truth-in-Lending statutes to disclose the APR of a loan, which allows borrowers a common ground for comparing various loans from different lenders.

Cash Flow

The amount of cash derived over a certain period of time from an income-producing property. The cash flow should be large enough to pay the expenses of the income producing property (mortgage payment, maintenance, utilities, etc.).

Closing

The meeting between the buyer, seller and lender or their agents where the property and funds legally change hands, also called settlement. Closing costs usually include an origination fee, discount points, appraisal fee, title search and insurance, survey, taxes, deed recording fee, credit report charge and other costs assessed at settlement. The costs of closing usually are about 3 percent to 6 percent of the mortgage amount.

Construction loan

A short term interim loan to pay for the construction of buildings or homes. These are usually designed to provide periodic disbursements to the builder as he progresses

Debt Service

The payments consisting of amortization and interest on a loan.

Depreciation

A loss from the upper limit of value caused by deterioration and/or obsolescence.

Discount

Newly-issued bonds are typically sold at some sort of **Discount**. So a bond that has a face value of \$1,000 and sells for \$925 has a \$75 discount. When interest rates rise, bonds are discounted more because you need a less expensive bond to achieve the same interest rate.

Equity

Your share of ownership in a property. Investors are often referred to as equity investors, because they invest in the equity of a property

First Mortgage

A **First Mortgage** is a mortgage that takes priority over all other voluntary liens.

Fixed Rate Mortgage

The mortgage interest rate will remain the same on these mortgages throughout the term of the mortgage for the original borrower.

Foreclosure

Foreclosure is the legal action taken to extinguish a home owner's right and interest in a property, so that the property can be sold in a foreclosure sale to satisfy a debt.

Interest

Interest is money charged for the use of borrowed funds. Usually expressed as an interest rate, it is the percentage of the total loan charged annually for the use of the funds.

Loan-to-Value Ratio

The **Loan-to-Value Ratio** is the ratio of the amount of money you wish to borrow compared to the value of the property you wish to purchase. Institutional investors (who buy loans on the secondary market from your mortgage company) set up certain ratios that guide lending practices. For example, the mortgage company might only lend you 80 percent of a property's value.

Lock-In

A **Lock-In** is the mechanism by which a borrower locks in the interest rate that will be charged on a particular loan. Usually, the lock lasts for a certain time period, such as 30, 45, or 60 days. On a new construction, the lock may be much longer.

Mortgage

A **Mortgage** is a document granting a lien on a home in exchange for financing granted by a lender. The mortgage is the means by which the lender secures the loan and has the ability to foreclose on the home.

Mortgage Banker

A **Mortgage Banker** is a company or a corporation, like a bank, that lends its own funds to borrowers in addition to bringing together lenders and borrowers. A mortgage banker may also service the loan (i.e., collect the monthly payments).

Net Operating Income

The income after deducting from gross income the operating expenses, including property taxes; insurance; utilities; management fees; heating and cooling expenses; repairs and maintenance; and replacement of equipment.

Operating Expenses

Generally speaking, all expenses, occurring periodically, that are necessary to produce net income before depreciation. Under some conditions these expenses are placed in two categories: operating expenses and fixed charges.

Point

A Point is one percent of the loan amount.

Real Estate Investment Trust (REIT)

A company dedicated to owning and, in most cases, operating income-producing real estate, such as apartments, shopping centers, offices and warehouses. Some REITs are also engaged in financing real estate. To be a REIT, a company is legally required to pay virtually all of its taxable income (95%) to its shareholders every year.

Tax Credit

A **Tax Credit** is an amount by which tax owed is reduced directly. In other words, a dollar-for-dollar amount is subtracted directly from the taxes you owe.

Tax Deduction

A **Tax Deduction** is an amount by which your income is reduced for the purpose of calculating taxes owed. In other words, this is a reduction in the percentage of income on which taxes are ultimately paid.

Time Value of Money

The concept underlying compound interest: that a dollar received today is worth more than a dollar in the future, due to opportunity, cost, inflation and certainty of payment.