KW *Commercial Real Estate*

Presents

<u>Commercial Real Estate – Sales, Leases / Lease Terms</u>

A general review of some common commercial real estate sales & leasing terms:

Tenant = Lessee **Owner = Lessor**

There are several major type leases in use today. These include:

*** Gross (Many variations) * Net * Percentage * Ground**

*** Sub * Assignment * Turnkey * Build-to-suit**

*** Sale-leaseback**

The following definitions are generally accepted in the industry. There are nuances and exceptions in the interpretation and application of the terms relative to a specific lease/property. Variations can occur geographically as well as to the accepted meaning in real practice in one part of the country vs. the other.

Abatement: A reduction or decrease; usually applies to the forgiveness of rent or a decrease of assessed valuation of ad valorem taxes after the assessment and levy.

Abated Rent: In the event of default – an owner can sue a tenant for repayment of abated rent.

Above Building Standard: Specialized design and engineering services and all construction necessary to personalize tenant space.

Absolute Net: **Lease** requiring tenant to pay in addition to base rent all costs associated with the operation, repair and maintenance of the building, all real estate taxes, and utilities including repair and maintenance of the building's structure and roof. Often the tenant is directly responsible both for all such costs and for the active handling of the items themselves. Distinguished from Triple Net (see below) by tenant's responsibility for maintenance and repair of the building structure and roof.

Absorbed Space: Net change in leased space between two dates.

Absorption: (1) The rate at which land or buildings will be sold or leased in the marketplace during a predetermined period of time, usually a month or a year. (2) The filling of space such as the rental of units or sale of a tract. The time or rate must be estimated and considered as part of the owner's (usually the builder) costs.

Absorption Period: The number of months required to convert vacant space into leased space assuming there is no new delivered space. Computed by dividing the average monthly absorbed space during a recent period by the current vacant space.

Acre: A tract of land consisting of 43,560 SF; A section contains 640 acres.

Acceptance: The date when both parties, seller and buyer, have agreed to and completed signing and/or initialing the contract.

Accumulated Cost Recovery: Total cost recovery deductions taken throughout the holding period of a property.

Active Income: Income from salary, wages, tips, commissions and activities in which the taxpayer materially participates. Also see passive income.

ADA: Americans With Disabilities Act passed by Congress in 1994 with intent to provide persons with disabilities accommodations and access equal to or similar to that of the general public.

Addendum: Something Added. A list or document or other material added to a document, lease, contract, letter, etc. IE: Legal description; List of FF&E; Survey; Map; Improvements to be made; etc.

Add-on Factor: Considered a loss factor, the % of gross rentable square footage that is lost due to the tenant's physical occupancy. The ratio of rentable to useable square feet. Also known as the load factor and the rentable-to-useable ratio. Also see efficiency percentage. Formula: Add-on factor =Rentable square feet divided by Useable square feet

Add Value: Fourth stage of four-stage transaction management process pertaining to a transaction manager's planning, effort, and continual contact with key decision-makers, investors, and users, as well as contact with ancillary professionals. This ongoing process allows for feedback, establishes a network for problem solving, provides a means to offer additional services to the client, and enhances the transaction manager's preparedness for the next assignment.

Adjusted Basis: The original cost basis of a property plus capital improvements, less total accumulated cost recovery deductions, and partial sales taken during the holding period.

Ad Valorem: (According to value) Used in reference to general property tax, which is usually based on the official valuation of property.

Agent: One who is authorized to act for or represent another (principal) usually in business matters. Authority may be express or implied.

Air Rights: The rights to use the air space over a piece of property.

Alienation Clause: A type of acceleration clause where a debt becomes due in its entirety upon the transfer of ownership of a secured property. See also "Due on Sales Clause" and "Acceleration Clause".

Allowance: A set dollar amount provided by the Landlord under a lease to be used by the Tenant for a specific purpose. Examples include allowances for tenant improvements; moving expenses design fees, etc. If the expense exceeds the allowance amount, such excess is the Tenant's responsibility. If the expense is less than the allowance, the savings are retained by the Landlord unless their agreement specifies otherwise.

Allowance Over Building Shell: One of three arrangements often used for financing tenant improvements (finishing out office space to accommodate a tenant such as walls, doors, carpeting, etc.). Often used in a yet-to-be-built building, this arrangement caps the landlord's expenditure at a fixed dollar amount over the negotiated price of the base building shell. This arrangement is most successful when both parties agree on a detailed definition of what construction is included and at what price. Tenants may ask for a contingency in the event the actual build-out costs are less than the allowance, requiring the landlord to return the savings in the form of rent abatement or other concession.

Amendment: A document to reflect a change either to correct an error or alter a part of an agreement without changing the principal idea or essence.

Amortization: Payment of debt in regular, periodic installments of principal and interest, as opposed to interest only payments. May also be used in a lease where the landlord incurs costs for additional tenant improvements which are effectively treated as a debt and repaid by tenant over the term of the lease.

Anchor Tenant: The most reliable, and usually the largest, tenant in a shopping center (or could be an office building or industrial building) the strength of the anchor tenant greatly affects the availability of financing for the property. May dramatically affect the attraction to the property of other tenants.

Anticipatory Breach: Occurs when one party to a contract, prior to time of performance, informs the other of his or her intent not to perform. Example: The buyer informs the seller before the closing date of his or her intent not to buy.

Annual Debt Service: (ADS) The total amount of principal and interest to be paid each year to satisfy the obligations of a loan contract.

Annual Percentage Rate: (APR) continued but interest is charged at the beginning of the year), but not the actual expenses incurred by the lender in making the loan and recharged to the borrower. (Encyclopedia of Real Estate Terms 2nd Edition, Damien Abbott)

Annuity: Regular fixed payments or receipts over a designated period of time.

Appreciation: An investment's increase in value.

Appreciation Potential: The possibility or probability that a real estate investment will increase in value during the holding period.

Appraisal: The estimation and opinion of value placed upon a piece of land based upon a factual analysis by a qualified professional; the process of estimation and the report itself.

Appreciation: An increase in the value of property caused by an improvement or the elimination of negative factors.

Arbitration Clause: A clause in a lease calling for the decision of a 3rd party (arbiter) regarding disputes over future rents based on negotiation. Also used in construction contracts, disputes between brokers, etc.

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As Is: As Is Condition – Premise accepted by buyer or tenant in the condition existing at the time of the sale or lease, including all physical defects.

Asking Rent: The dollar amount asked by landlords for direct available space (not sublease), expressed in dollars per square foot per year in most parts of the country and dollars per square foot per month in areas of California and selected other markets. Buildings will have an average asking rent for available space. Usually a point of departure for negotiations between landlords and tenants.

Assessment: (1) An estimate of property value for the purpose of imposing taxes. (2) A fee imposed on property, usually to pay for public improvements such as streets and sewers.

Asset Based Lender: A lender who loans money based primarily on the values of an asset - accounts receivable, inventory, a piece of equipment real estate – rather than on the financial strength of the business, which is the primary criterion for banks.

Assessed Value: The value of real property established by the tax assessor for the purpose of levying real estate taxes.

Assignment: Under the terms of an assignment, a tenant transfers all interest in the leased property to another party. Generally all lease terms remain the same. To transfer interest in a property.

Attachment: Legal procedure to add in the collection of a debt. Usually the court issues a writ to seize the property of a debtor and holds it pending the outcome of a lawsuit, keeping the property available for sale to pay any money judgment entered in such lawsuit.

Attorn: To turn over or transfer to another money or goods. To agree to recognize a new owner of a property and to pay him rent. See also Letter of Attornment.

Average Annual Effective Rate: The average annual effective rent divided by the square footage.

Average Annual Effective Rent: The tenant's total effective rent divided by the lease term.

Averaging Method: A simple technique used to forecast next period's/year's vacancy rate by averaging previous years' vacancy rates; especially effective where vacancy rates have remained relatively flat or show little variability over time.

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Back Up Offer: A secondary offer to buy property. Used in case the first offer (primary) fails. A back up offer is especially useful when the primary offer contains difficult contingencies, time frames, finance issues, etc.

Balloon Payment: A large payment due on a balloon note. Generally a balloon payment is required when regular monthly or quarterly payments have not covered both the increase due and the principal of the loan.

Base Rent: A specific amount used either as a minimum rent in a lease (retail) which uses a percentage of sales or overage for additional rent or sets a base onto which is added expenses and taxes in a net lease or increases in those items in a fully serviced lease. May contain provisions to increase the base rent amount over the term of the lease to account for the time value of money.

Base Year: The year upon which a direct expense calculation of rent is based. The 12 month period upon which a direct expense escalation of rent is based. Typically the calendar year the lease commences. AKA "dollar stop lease". Used typically in FSG, MG and IG leases (Full Service, Modified, Industrial Gross leases), tenant pays expenses over and beyond those experienced in the first year / base year.

Below Grade: Any facility or part of a facility located underground or below the surface grade.

Big Boxes: A retail real estate slang term for large square footage tenants such as Wal-Mart, a grocery store, a department store, a Home Depot or Lowes, etc.

Bill of Sale: Document used to transfer title (ownership) of personal property.

Breakpoint: A retail business term that specifies the point when a tenant would pay additional rent based upon a % of sales.

Breach of Warranty: The failure of the seller of real property to pass title as either express or implied by law in the conveyancing document.

Bridge Loan: A bridge loan is a short-term loan used until a person or company secures permanent financing or removes an existing obligation. This type of financing allows the user to meet current obligations by providing immediate cash flow. The loans are short term, up to one year, with relatively high interest rates and are usually backed by some form of collateral such as real estate or inventory.

BREAKING DOWN 'Bridge Loan'

Also known as interim financing, gap financing or swing loans, bridge loans "bridge the gap" during times when financing is needed but is not yet available. Both corporations and individuals use bridge loans, and lenders can customize these loans for many different situations.

Broker: Common term used to refer to any commercial real estate licensee. In many states – denotes a level of license held – ie: Sales Agent vs. Broker.

Buffer: A strip or parcel of land established as a transition between parcels of land, such as a strip or parcel of land between an industrial and residential area. May contain natural or planted shrubs, walls or fencing, singly or in combination. Also known as Buffer Zone or Buffer Strip.

Building Classifications: Class A – Building has excellent location and access to attract the highest quality tenants. Building must be of superior construction and finish, relatively new or competitive with new buildings and providing professional on-site management. Class B- Building with good location, management, construction land tenancy. Can compete at low end of Class A. Class C – Generally an older building with growing functional and/or economic obsolescence. Class D – An older building in need of extensive renovation as a result of functional obsolescence or deterioration.

Building Code: Local, state, or regional ordinances that specify various methods and materials to be used to construct improvements to comply with requirements.

Building Core: The central or arterial part of a multistory building that integrates functions and service needs for established occupants. Such areas are normally composed of toilet facilities, elevator banks, janitorial closets, utilities, mechanical facilities, stairwells, etc. (See Core Factor)

Build-out: The cost of configuring and finishing new or relet space in accordance with a tenant's specifications.

Building Standard: A list of construction materials and finishes used in building out office space for a tenant that the landlord contributes as part of the tenant improvements. Examples of standard building items are doors, partitions, lights, floor covering, telephone outlets, etc. May also specify the quantity and quality of the materials to be used and often carries a dollar value.

Build-To-Suit: Under the terms of a build-to-suit option, a landlord agrees to develop or finish a property or space to the specifications of a tenant. Building costs are usually offset, in part, by increased rent paid by the tenant. This option is seen in the case of a general-purpose industrial building with special-use attributes.

Bumps: Negotiated increases in the base rent that occur throughout the term of the lease. Can be in any amount – either $ or % and at any interval(s) as may be agreed upon by all parties. IE: Every anniversary / annually, etc.

CAM: Common area maintenance

CAM Charges: Common Area Maintenance charges. Those charges levied on or the expenses incurred in maintaining the common areas of a building.

Cancellation Clause: A provision in a lease that confers upon one or both of the parties to the lease the right to terminate the lease upon the occurrence of the condition or contingency set forth in the clause – terms negotiable.

Capitalization: A process of determining the value of real property in which project income is divided by a predetermined annual rate (capitalization rate). For example, a building with annual project income of $100,000 is worth $1,000,000 at a 10% Cap Rate ($100,000 / 10% =$1,000,000

Cap Rate: Cap Rate is a term used to calculate and thus indicate the value of a property. Probably the most common, and therefore effective, method to value an investment is through the use of a cap rate. Cap Rate is the rate of return used to determine the value of the property's income stream. Precisely defined, the cap rate is the net operating income of the property divided by its purchase price. It shows the expected percent annual return given a specific investment

The Capitalization Rate: The NOI divided by the purchase price reflects a Cap Rate

The Cap Rate is calculated as follows:
Cap Rate = (Net Operating Income / Market Value) x 100
Cap Rate = (NOI / MV) x 100

Example:

Net Operating Income (NOI): $239,430

Market Value (MV): $3,420,000
Cap Rate = (239,430 / $3,420,000) x 100
Cap Rate = 7%
The Cap Rate of 7% represents the annual return before mortgage payments and income taxes on the total investment of $3,420,000.

What You Should Know About The Cap Rate

The capitalization rate is a fundamental concept in the commercial real estate industry. Yet, it is often misunderstood and sometimes incorrectly used. This post will take a deep dive into the concept of the cap rate, and also clear up some common misconceptions.

Cap Rate Definition

What is a cap rate? The capitalization rate, often just called the cap rate, is the ratio of Net Operating Income (NOI) to property asset value. So, for example, if a property was listed for $1,000,000 and generated an NOI of $100,000, then the cap rate would be $100,000/$1,000,000, or 10%.

$$\text{Capitalization Rate} = \frac{\text{annual net operating income}}{\text{cost (or value)}}$$

Cap Rate Example

Let's take an example of how a cap rate is commonly used. Suppose we are researching the recent sale of a Class A office building with a stabilized Net Operating Income (NOI) of $1,000,000, and a sale price of $17,000,000. In the commercial real estate industry, it is common to say that this property sold at a 5.8% cap rate.

Intuition Behind the Cap Rate

What is the cap rate actually telling you? One way to think about the cap rate intuitively is that it represents the percentage return an investor would receive on an all cash purchase. In the above example, assuming the real estate proforma is accurate, an all cash investment of $17,000,000 would produce an annual return on investment of 5.8%. Another way to think about the cap rate is that it's just the inverse of the price/earnings multiple. Consider the following chart:

Cap Rate	12.00%	11.00%	10.00%	9.00%	8.00%	7.00%	6.00%
Multiple	8.33	9.09	10.00	11.11	12.50	14.29	16.67

As shown above, cap rates and price/earnings multiples are inversely related. In other words, as the cap rate goes up, the valuation multiple goes down.

When, and When Not, to Use a Cap Rate

The cap rate is a very common and useful ratio in the commercial real estate industry and it can be helpful in several scenarios. For example, it can and often is used to quickly size up an acquisition relative to other potential investment properties. A 5% cap rate acquisition versus a 10% cap rate acquisition for a similar property in a similar location should immediately tell you that one property has a higher risk premium than the other.

Another way cap rates can be helpful is when they form a trend. If you're looking at cap rate trends over the past few years in a particular sub-market then the trend can give you an indication of where that market is headed. For instance, if cap rates are compressing that means values are being bid up and a market is heating up. Where are values likely to go next year? Looking at historical cap rate data can quickly give you insight into the direction of valuations.

While cap rates are useful for quick back of the envelope calculations, it is important to note when cap rates should not be used. When properly applied to a stabilized Net Operating Income (NOI) projection, the simple cap rate can produce a valuation approximately equal to what could be generated using a more complex discounted cash flow (DCF) analysis. However, if the property's net operating income stream is complex and irregular, with substantial variations in cash flow, only a full discounted cash flow analysis will yield a credible and reliable valuation.

Components of the Cap Rate

What are the components of the cap rate and how can they be determined? One way to think about the cap rate is that it's a function of the risk free rate of return plus some risk premium. In finance, the risk free rate is the theoretical rate of return of an investment with no risk of financial loss. Of course in practice all investments carry even a small amount of risk. However, because U.S. bonds are considered to be very safe, the interest rate on a U.S. treasury bond is normally used as the risk-free rate. How can we use this concept to determine cap rates?

Suppose you have $10,000,000 to invest and 10-year treasury bonds are yielding 3% annually. This means you could invest all $10,000,000 into treasuries, considered a very safe investment, and spend your days at the beach collecting checks. What if you were presented with an opportunity to sell your treasuries and instead invest in a Class A office building with multiple tenants? A quick way to evaluate this potential investment property relative to your safe treasury investment is to compare the cap rate to the yield on the treasury bonds.

Suppose the acquisition cap rate on the investment property was 5%. This means that the risk premium over the risk free rate is 2%. This 2% risk premium reflects all of the additional risk you assume over and above the risk free treasuries, which takes into account factors such as:

- Age of the property.
- Credit worthiness of the tenants.
- Diversity of the tenants.
- Length of tenant leases in place.
- Broader supply and demand fundamentals in the market for this particular asset class.
- Underlying economic fundamentals of the region including population growth, employment growth, and inventory of comparable space on the market.

When you take all of these items and break them out, it's easy to see their relationship to the risk free rate and the overall cap rate. It's important to note that the actual percentages of each risk factor of a cap rate and ultimately the cap rate itself are subjective and depend on your own business judgement and experience.

Is cashing in your treasuries and investing in an office building at a 5% acquisition cap rate a good decision? This of course depends on how risk averse you are. An extra 2% yield on your investment may or may not be worth the additional risk inherent in the property. Perhaps you are able to secure favorable financing terms and using this leverage you could increase your return from 5% to 8%. If you a more aggressive investor this might be appealing to you. On the other hand, you might want the safety and security that treasuries provide, and a 3% yield is adequate compensation in exchange for this downside protection.

Band of Investment Method

The above risk free rate approach is not the only way to think about cap rates. Another popular alternative approach to calculating the cap rate is to use the band of investment method. This approach takes into account the return to both the lender and the equity investors in a deal. The band of investment formula is simply a weighted average of the return on debt and the required return on equity. For example, suppose we can secure a loan at an 80% Loan to Value (LTV), amortized over 20 years at 6%. This results in a mortgage constant of 0.0859. Further suppose that the required return on equity is 15%. This would result in a weighted average cap rate calculation of 9.87% (80%*8.59% + 20%*15%).

The Gordon Model

One other approach to calculating the cap rate worth mentioning is the Gordon Model. If you expect NOI to grow each year at some constant rate, then the Gordon Model can turn this constantly growing stream of cash flows into a simple cap rate approximation. The Gordon Model is a concept traditionally used in finance to value a stock with dividend growth:

$$\text{Value} = \frac{\text{CF}}{\text{k} - \text{g}}$$

This formula solves for Value, given cash flow (CF), the discount rate (k), and a constant growth rate (g). From the definition of the cap rate we know that Value = NOI/Cap. This means that the cap rate can be broken down into two components, k-g. That is, the cap rate is simply the discount rate minus the growth rate.

How can we use this? Suppose we are looking at a building with an NOI of $100,000 and in our analysis we expect that the NOI will increase by 1% annually. How can we determine the appropriate cap rate to use? Using the Gordon Model, we can simply take our discount rate and subtract out the annual growth rate. If our discount rate (usually the investor's required rate of return) is 10%, then the appropriate cap rate to use in this example would be 9%, resulting in a valuation of $1,111,111.

The Gordon Model is a useful concept to know when evaluating properties with growing cash flows. However, it's not a one-size fits all solution and has several built in limitations. For example, what if the growth rate equals the discount rate? This would yield an infinite value, which of course in nonsensical. Alternatively, when the growth rate exceeds the discount rate, then the Gordon Model yields a negative valuation which is also a nonsensical result.

These built-in limitations don't render the Gordon Model useless, but you do need to be aware of them. Always make sure you understand the assumptions you are making in an analysis and whether they are reasonable or not.

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Carrying Charges: Various costs that are incidental to property ownership (taxes, insurance costs, maintenance expenses); Costs involved in keeping a property which is intended to produce income but has not done so as of yet.

Cash on Cash Return:

Another measure of property value. Also called equity dividend return. This formula enables investors to determine the return on their equity in Leverages properties. Cash on Cash =before tax cash flow (NOI minus Debt service) divided by initial cash outlay

Example: Assume initial cash investment to purchase a property was $100,000 and your NOI this year after mortgage payments was $25,000. Your return would be 25%.

The same formula can be used to calculate after-tax return. Just subtract both the mortgage payment and the estimated taxes from your NOI.

Divide cash flow after debt service by the total purchase price.

Cash-on-cash return = Annual Before Tax Cash Flow
Divided by: Total Cash Invested

$1,200,000 Apartment Complex Purchase Price
300,000 Downpayment
5,000 Monthly Cash Flow From Rentals Less Expenses
60,000 Annual Cash Flow From Rentals Less Expenses

Cash on Cash = $60,000 divided by $300,000 = 0.20 = 20%

Limitations

- Because the calculation is based solely on before-tax cash flow relative to the amount of cash invested, it cannot take into account an individual investor's tax situation, the particulars of which may influence the desirability of the investment. However the investor can usually deduct enough Capital Cost Allowance to defer the taxes for a long time.
- The formula does not take into account any appreciation or depreciation. When some cash is a return of capital (ROC) it will falsely indicate a higher return, because ROC is not income.
- It does not account for other risks associated with the underlying property.
- It is essentially a simple interest calculation, and ignores the effect of compounding interest. The implication for investors is that an investment with a lower nominal rate of compound interest may be superior, in the long run, to an investment with a higher cash-on-cash return.

It is possible to perform an after-tax Cash on Cash calculation, but accurate depictions of your adjusted taxable income are needed to correctly address how much tax payment is being saved through depreciation and other losses.

Cash on Cash – Examples:

Definition: *The amount of cash that is returned by the property to the investor in the first year compared to acquisition costs expressed in percentages.*

To calculate Cash-on-Cash (COC), divide the amount of money received (Came IN) Year One by the total amount invested (Went OUT). This is expressed in percentages.

Formula: $\frac{\textbf{Annual before-tax cash flow}}{\textbf{Total cash invested}}$ **= Cash-on-Cash return**

Example #1: it costs a total of $75,000 to close your deal. Your deal threw off $75,000 in income. Return? 100%! How to calculate?

$\frac{\$75{,}000 \text{ (came IN)}}{\$75{,}000 \text{ (went OUT)}} = 1.00 \text{ or } 100\%$

Example #2: it costs $75,000 to close your deal. It throws off $37,500 in income:

$\frac{\$37{,}500 \text{ (came IN)}}{\$75{,}000 \text{ (went OUT)}} = .50 \text{ or } 50\%$

Example #3: it costs $75,000 to close your deal. It throws off $15,000 in income:

$\frac{\$15{,}000 \text{ (came IN)}}{\$75{,}000 \text{ (went OUT)}} = .20 \text{ or } 20\%$

How do you use this?
This measurement tells you when you get your money back!
At 100% cash-on cash you will receive your total investment back in ONE year; at 50% COC - in TWO years; at 20% COC - in FIVE years.

Consider this measurement in conjunction with all the other measurements to determine if the investment you are considering meets your investment criteria. For me personally: I am not so much concerned about the return ON my investment as I am about the return OF my investment. I want my money back soon so i can reinvest it. Your money needs to keep working for you.

Cash Flow: The cash an owner has left after paying operating expenses and debt service.

CFBT Cash Flow Before Tax – cash available after paying all operating expenses but before paying taxes (income taxes)

Formulation

Net Operating Income
- Debt Service
- Capital Additions
+ Loan Proceeds
+ Interest Earned
= Cash Flow Before Taxes

Example

Say a rental property generates a net operating income of $120,000, requires the investor to make an annual mortgage payment of $100,000 (the debt service), and that there are no capital additions, additional loan proceeds, or interest earned.

Result

$120,000
- 100,000
- 0
+ 0
+ 0
= 20,000

CFAT Cash Flow After Tax – cash available after paying all operating expenses and paying tax obligations (income taxes)

This is a bit more complex because it requires a calculation for taxable income followed by a computation for income tax liability (or loss) which in turn is subtracted from CFBT. We'll start with the formulation then look at the two other components required to make the calculation. For this discussion, however, we will keep it simple because we are just trying to give you an idea of how it works. There are other articles here on the subject with more detail if you wish.

Formulation

Cash Flow Before Taxes
- Tax Liability
= Cash Flow After Taxes

Okay, so we have to see how the tax liability is computed in order to make the calculation. We will show you both formulations and then add some assumptive numbers to arrive at a result.

Net Operating Income
- Interest Expense (mortgages)
- Amortized Points (mortgages)
- Depreciation (real property and capital additions)
+ Interest Earned
= Taxable Income

then,

Taxable Income
x Marginal Tax Rate (investor's combined state and federal tax rates)
= Tax Liability

To complete the calculation so we can show you the final result will assume that the tax liability is $7,000 and refer back to the amount we arrived at previously for cash flow before taxes.

Result

$20,000
- 7,000
= 13,000

Note: In this illustration we assumed that the investor had a tax liability and therefore it was subtracted from the cash flow before taxes. Had it been a tax savings, however, it would have been added instead. In other words, had the taxable income resulted in a negative amount, then that amount would have become an income tax savings which would have increased cash flow after tax.

Certificate of Insurance: A certificate issued by an insurance company or its agent. It verifies that a certain insurance policy is in effect for stated amounts and coverage and names those insured. Coverage should be – at a minimal – that which is called for in the lease document.

Certificate of Occupancy:

Many cities / municipalities require a new tenant to obtain a Certificate of Occupancy. The lease term should stipulate who is responsible for obtaining the C/O in order to permit legal occupancy of the property. If modifications are required to obtain a C/O - who is responsible for compliance.

Change Order: An order issued any time there is a change in the specification, price or time set forth in the building contract as authorized by the owner, architect or engineer. May incur an additional charge to accommodate same.

Class: Class is usually used in conjunction with an office property and refers to the quality of property. Class definitions fall with the following guidelines. **Class A+:** Landmark quality, high rise building with prime central business district location (the best of the Class A buildings). **Class A:** Generally 100,000 sf or larger (five or more floors), concrete and steel construction, built since 1980, business/support amenities, strong identifiable location/access. **Class B:** Renovated and in good locations. Newer building are smaller in size, wood frame construction, and/or in non-prime location. **Class C:** Older, un-renovated of any size in average to fair condition.

Clear Span Facility: A parking structure with vertical columns on the outside edges of the structure and a clear space between columns, making it unnecessary for vehicles to maneuver between columns.

Client: A buyer or seller who is represented by a real estate licensee.

Cloud on Title: Any condition that affects the clear title to real property.

Co-Brokerage Agreement: Agreement between brokerage firms on how the commission will be shared and paid.

COLA: Cost of living adjustment to the base rent

Commencement Date:

The date on which a lease begins. This is typically but not always the day on which the tenant takes possession of the leased space, which usually occurs upon substantial completion of the tenant improvements. (See Occupancy Date). (See Rent Commencement) The commencement date and date of possession can be the same in the event the tenant is to perform the desired repairs, maintenance, improvements, etc. and in turn may receive a period of “free” rent or rental abatement. In that case – Possession and Lease Commencement are one and the same. After the free rent period comes the Rent Commencement date which is the date called for in the lease for the tenant to commencement payment of rent. In some cases the tenant may have already paid the actual first month’s rent even though it may be for a period that is several months after Possession or Lease Commencement. In that case – the tenant’s next obligation to pay rent is the month thereafter.

Common area factor:

This is a term that defines commonly shared, public space within buildings (usually office buildings). This can include hallways, Vestibules, rest rooms, lobbies and atriums. The factor is usually described as a percentage and should be accounted for in your space allocation. For example, you may be using 1,500 usable square feet, but if the common area factor is 15 percent, then your rentable square feet is 1,725 square feet. Other buildings may be different, so be careful when comparing your effective rental rate.

Common Area Maintenance: (CAM)

The cost of maintaining the exterior and/or the shared interior areas of a property may be passed through form the landlord to a tenant. These costs may include snowplowing, rubbish removal, parking lot lighting, cleaning of restrooms. Property management, taxes and other costs. It is important to identify the amount of these costs, which is included in the rent (also known as "stops") which may increase or decrease over time

Comparable: A term used in real estate, often times appraisals, where a comparable property, recently sold or leased, that an appraiser or broker can use as a comparison to the one they are trying to value.

Competition: Restricts landlord's right to lease nearby space to businesses similar to those of the tenant's. This clause is usually found in leases of retail space. "No Compete" or tenant receives "exclusive right" to represent / provide a particular type of service / product in the property.

Compliance With the Federal Americans with Disabilities Act (ADA):

States that the building complies with the ADA . This is important because both the tenant and the landlord are responsible for making the property accessible to disabled persons. The tenant should make sure that the landlord makes this warranty based on an ADA survey or an audit performed by an engineer or architect. In many cases - as older properties become available - they will be required to be made to be in compliance with ADA standards. Some exceptions apply.

Concessions: Cash (or cash equivalents) expended by the landlord in the form of rent abatement, build-out allowance, moving expenses, or other payments to induce the tenant to sign a lease.

Condemnation: The process by which private property is taken by a governmental agency for public use without the consent of the owner, but only upon payment of just compensation. See also Eminent Domain.

Conditional Contract: A contract with conditions that must be met before a party has to perform.

Consideration: Anything of value to induce another to enter into a contract, ie: money, services, a promise.

Construction Management: An arrangement for building construction whereby the owner engages a contractor to oversee the work of all building trades, each of which enters a separate construction contract with the owner. By contrast – see General Contractor.

Consumer Price Index (CPI): A federal government index that measures the change in the cost of a variety of goods and services. Used in loans, purchase agreements and leases as a measure by which to adjust future payments to reflect inflation. Also called "Cost of Living Index)

Contiguous Space: Adjoining office space. Multiple offices/retail spaces or blocks of spaces that can be combined and rented to a single tenant. Can also be on multiple floors in a highrise building.

Contract Documents: The design plans and specifications for construction of a facility. Working drawings that detail for the contractor the exact manner in which a project should be built.

Contract Rent: Rent paid under a lease. The actual rent as opposed to the market rental value of the property.

Conveyance: Most commonly refers to the transfer of title to land between parties. The term may also include most of the instruments by which an interest in real estate is created, mortgaged or assigned.

CORE FACTOR: A term used to denote an add on to the square footage of an office space to allow for the owner to recoup the costs associated with providing space in a building for hallways, stairwells, elevators, restrooms, break rooms, etc. If an office space is 500 SF with a core factor of 15% - the tenant pays based on a rental rate factor calculated on 575 SF.

Cost Approach: A method of appraising real property whereby the replacement cost of a structure is calculated using current costs of construction.

Covenant: A private, legal restriction on the use of land recorded in the land records.

Covenant of Quiet Enjoyment: Usually inserted in leases or conveyances whereby landlord or grantor promises that the tenant or grantee shall enjoy possession of the premises in peace and quiet without disturbance.

CPM: Certified Property Manager – A designation awarded through the Institute of Real Estate Management – a division of the NAR – for those who have achieved a level of knowledge and experience in the professional management of real properties. www.irem.org

CPI: Consumer Price Index – an index that provides a means to make adjustments to the base rent based on any increases to the index which is based on certain costs to a list of expenses typical to a consumer.

CRE: Counselor of Real Estate - The Counselors of Real Estate is the membership organization established exclusively for real estate advisors who provide intelligent, unbiased, and trusted advice for a client or employer. www.cre.org

Cumulative Discount Rate: A discount factor applied to the rental rate that takes into effect all landlord lease concessions expressed as a % of base rent.

CUP: Conditional Use Permit – required to change the use of a property to something other than specified zoning.

Daisy Chain: A term used typically in commercial loan transactions (not so much in residential) whereby a borrower may be purchasing a property – likely a distressed property that does not qualify for conventional loans – and contacts a mortgage loan broker for assistance. That initial loan broker may not have a direct source for such a loan but then contacts another broker. There could be 2, 3, 4, 5 of these involved in a transaction. Each getting involved in the deal to help further it along and each wanting a fee out of for their assistance. The original borrower may have no idea how many are involved or how much such fees total up and to / for whom. Due to the nature of the property and the creditworthiness of the borrower – he may have no choice but to pursue this type of loan and pay for the fees involved to get the deal done. The term Daisy Chain is just a term to denote the parties that are tied to one another throughout the course of the loan transaction.

Dedicate: Transfer of property from private to public ownership.

Deed: Generally, a conveyancing instrument given by the seller to pass fee title to property upon sale.

Deed In Lieu of Foreclosure: A deed given by an owner/borrower to a lender to prevent the lender from bringing foreclosure proceedings.

Deed of Trust: An instrument securing a loan that is used in many states in place of a mortgage. Property is transferred to a trustee by the borrower (trustor), in favor of the lender (beneficiary), and re-conveyed to the borrower upon payment in full.

Debt Coverage Ratio: Debt Coverage Ratio (DCR) is the ratio between the mortgage payment and the amount of NOI available to pay mortgage debt service. Lenders require that the property meet both a loan to value and a debt coverage ratio in order to qualify for a loan.

Default: The omission or failure to perform a legal or contractual duty or to pay an obligation when due. Some specific examples are: Failure to make a payment of principal or interest or other type of financial obligation when due; the breach or failure to perform any of the terms of a note or the covenants of a mortgage or deed of trust.

Deficiency Judgment: Commonly, the amount for which the borrower is personally liable on a note and mortgage if the foreclosure sale does not bring enough to cover the amount owed. Actually, the judgment is for the total amount of the obligation and not for the deficiency. Any recoveries from a foreclosure sale are deducted from the judgment. May also apply to debt due after repossession of personal property subject to a security interest.

Delivered Buildings: Buildings that have completed construction and are ready for tenant build-out. May or may not yet have a C of O.

Demising Walls: The boundaries that separate a tenant's space from another tenant's space and from a public corridor.

Density: Number of dwelling units divided by the gross acreage being developed. For an urban project, this term is also used to refer to the Floor Area Ratio.

Design / Build: A system in which a single entity is responsible for both the design and construction of a facility, often involving the fast-track method of construction; also referred to as a Design/Construct.

Depreciation: Decrease in the usefulness and therefore value, of real property improvements or other assets caused by deterioration or obsolescence; A loss in value as an accounting procedure to use as a deduction for income tax purposes; Spreading out the cost of a capital asset over its useful life.

Rental property depreciation (also known as cost recovery) is one of the biggest tax deduction benefits real estate investors enjoy by owning rental properties.

The beauty of the rental property depreciation allowance lies in the fact that it is simply a "paper loss" the real estate investor can write off during each year the rental property is owned without having to shell a dime from out of pocket.

The investor can legally deduct an amount for depreciation as cost recovery each year from the cash flow he or she collected from the asset during the past twelve months of ownership and therein lower his or her tax liability for that past year. But unlike say, mortgage interest (which is also a legal tax deduction), real estate investors never have to fork out any money for depreciation on rental property.

Destruction or Condemnation:

States if the landlord is required to rebuild if the property is destroyed. This clause will specify whether the rent will be abated and whether or not the tenant can terminate the lease if the building is totally or partially destroyed. It will also specify the rights of the parties if the property is taken by eminent domain.

Discounted Cash Flow:

Discounted Cash Flows - also known as Net Present Value of Discounted Cash Flows is a valuation method which discounts future cash flows back to the present to estimate the attractiveness of an investment.

Discount Points: A loan fee charged by a lender to increase the yield on the investment. One point = 1% of the loan amount.

Distraint: The act of taking (legally or illegally) personal property and retaining control until the property owner performs an obligation. Commonly, a landlord takes possession of personal property of a tenant in default until the default is satisfied.

Distress Sale: The sale of property under less than favorable conditions. Usually, the seller is experiencing financial difficulties and is under extreme pressure to sell.

Dock High: A loading dock for trucks that allows them to offload directly onto floor level of a building. Can be a true dock high or could be a "well" whereby excavation is done to create an area where a truck can back into and offload to the floor level which is the ground level.

Dollar Stop: An agreed dollar amount of taxes and operating expense (expressed for the building as a whole or on a SF basis) over which the tenant will pay its prorated share of increases. May be applied to specific expenses (e.g., property taxes or insurance).

DOUBLE NET LEASE:

Tenant pays property taxes and insurance.

Due Diligence: The process you perform prior to having your purchase contract go "hard". It goes hard when you reach a point where you have something other than your time and inspection fees at risk – perhaps a deposit or a promise to close on the property without further inspections.

Earnest Money: A sum of money paid by a buyer at the time of entering a contract to indicate the intention and ability of the buyer to carry out the contract. Normally such earnest money is applied against the purchase price. The amount can be any amount agreed upon by the parties to the contract. Earnest money is NOT required to make a contract a valid contract.

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Easement: A right to use the property of another created by grant, reservation agreement, prescription, or necessary implication. It is either for the benefit of land appurtenant, such as the right to cross A to get to B or in gross, such as a public utility easement.

Economic Feasibility: A project's feasibility in terms of costs and revenue with excess revenue establishing the degree of feasibility.

Economic Rent: Calculations or analysis to determine market rental value of a property at any given time, even though the actual rent may be different.

Effective Date: The effective date is VERY important as it is the date from which all days, dates, time frames commence from. Here is how that date is determined:

The effective date is determined by the final date of acceptance. The final date of acceptance is the date on which the contract becomes binding between the Buyer and Seller, in other words, the date that both the Buyer and Seller have agreed to ALL terms of the contract and have executed the contract. Four elements must be satisfied for final acceptance to occur:

1. The final contract must be in writing.

2. The Buyer and Seller must sign the final contract, including the initialing of any handwritten changes to the initially drafted offer, if applicable.

3. Acceptance must be unequivocal, in other words, clear, having only one possible meaning, and with no shred of doubt.

4. The last party to accept must **communicate acceptance back** to the other party or the other party's agent.

The effective date is the date when the fourth element is made after the other three elements are satisfied. All contract performance requirements or periods of performance then begin to run.

Effective Rent: The average per square foot rent paid by the tenant over the term of a lease. Takes into account only free rent and stepped rents. Does not include allowances, space pockets, free parking and other similar landlord concessions.

Effective Useable Area:

Excludes those areas within the Useable Space (see below) that the tenant pays rent on but effectively cannot use such as columns and sharply angled spaces.

Efficiency Factor: The number resulting from dividing the Usable Area by the Gross Building Area in an office building, providing a benchmark measurement for the economic efficiency of that building's use as an office building.

Eminent Domain: A right of the government to acquire private property for a public use by condemnation in return for just compensation. See also condemnation.

Encroachment: Generally, a structure that extends impermissibly over a property line, easement boundary, or building setback line.

Encumbrance: Any right to, or interest in, real property that may exist in one other than the owner but which will not prevent the transfer of fee title. A claim, lien, charge, or liability attached to and binding real property.

Enforcement: Specifies how the agreement is to be enforced and who pays attorney fees. Many businesses negotiate a clause into leases requiring the parties to resolve any disputes through either mediation or arbitration.

Environmental Impact Report:

A report generally prepared by an independent company detailing the probable environmental effect of a development on the surrounding area.

Equity: The value of one's interest in a property consisting of its fair market value less any outstanding debt or other encumbrances.

Equity Kicker: Also called a participation loan. Under this kind of loan – often used by non-bank lenders with start-up businesses – the lender gets not only interest payments and principal repaid, but the right to buy equity (part ownership in the company) as well. Equity participation is generally required for riskier deals or in return for lower rates.

Equity Participation: The participation by a lender in the equity ownership of a project as one of the conditions for granting a loan. Used by financial institutions to partially offset the effects of inflation. Also called "Equity Kicker".

Equity of Redemption: Not the same as the redemption period after a foreclosure sale, which is a right established by payment of the principal, interest and costs due.

Escalation Clause: Provides for increases in rent over a specified period of time. Most commercial leases contain escalation clauses. Ascertain how the increase is determined. Is it keyed to actual increases in the landlord's operating costs or to some outside index?

Escrow Agreement: A written agreement (ie: contract) usually made between a buyer, seller and escrow agent (title company). The escrow agreement sets forth the basic obligations of the parties, describes the objects deposited in escrow and instructs the escrow agent concerning the disposition of the objects deposited.

Escrow Payment: That portion of a mortgagor's monthly payment held in trust by the lender to pay for taxes, hazard insurance and other items as they become due.

ESFR Sprinkler System: Early Suppression Fast Response – New technology fire sprinkler system offering faster response time, higher volume of water, larger water droplets for greater efficiency in fire detection and suppression even though the system is in the ceiling structure.

Estoppel Certificate:

An instrument which itself prevents individuals from later asserting facts different from those contained in the document. Often required by the buyer of an office building. The tenant and landlord both sign the Estoppel certificate, confirming the lease and pertinent facts thereto. Thereafter, neither party may make claims to the contrary.

Exchange: There are 2 basic types of tax free exchanges. 1031 and 1033. A 1031 exchange (named for the section in the IRS code where the rules are found) enables a property owner to sell a property (any type other than their residence) and purchase a like kind of property with the proceeds without the proceeds being taxed at that time. A seller can sell the likes of a piece of land, a retail building, an office building, an apartment building, land, etc. and then use the proceeds to purchase a different property. A key component here is that the seller cannot take possession of the funds – they must be handled by a 3rd party facilitator – a 1031 Tax Exchange Agent. There is also a 1033 exchange that involves property that is being sold as a result of action by eminent domain – or the real threat of same. Can also include property destroyed by fire, storm, etc. The rules are different for a 1033 than a 1031. Inquire for more info or seek competent counsel, advice, direction and guidance on either of these – insufficient space permitted to give extensive details here.

Exclusions: This would typically be a defined list of one or more business types that cannot locate in a retail center without the approval of the landlord as well as a tenant who has signed a lease that precludes certain uses from being in the same center.

Exclusive: A tenant – typically retail but could be in office or industrial property – that has an exclusive right clause in their lease that would preclude any other similar tenant from being placed in the same property. Conversely – in leasing space in a property – you have to know if there are exclusive clauses that would prohibit another similar tenant from being placed in a property.

Expansion: Gives the tenant the right to add adjacent space or to move into a larger vacant space in the building

Expenses: Leases in the DFW area generally assume that there are six (6) different types of expenses: Roof and Structure; Taxes; Insurance; Utilities; Janitorial (excluding outside trash removal); Common Areas (utilities and general maintenance) and Electricity. Variables would be for water / sewer expenses.

Expense Stop: A fixed amount (typically per square foot) in a lease where the tenant is responsible for all building operating expenses and taxes in excess of said amount. May be applied to specific expense – taxes / insurance. There can also be a "cap" in that tenant pays expenses over / above the stop but there can be a limit to the amount – either in a $ amount or a % of increase – not to exceed.

Extension Option: An agreed continuation of occupancy under the same conditions, as opposed to a renewal, which implies new terms or conditions. In a lease, it is a right granted by the landlord to the tenant whereby the tenant has the option to extend the lease for an ad.

FAR: Floor Area Ratio – calculated as a ratio of the footprint of the built surface area, to the total size of a property.

Face Rental Rate: The "asking" or nominal rental rate published by the landlord.

Fair Market Rent: The rent which would be normally agreed upon by a willing landlord and tenant in an "arm's length transaction" for a specific property at a given time, even though the actual rent may be different. In a lease, the term "fair market rent" is defined in a number of different ways and is subject to extensive negotiation and interpretation.

Feasibility Study: An analysis of needs, costs of recommended improvements and anticipated revenue and costs; establishes the basis for the construction of an individual improvement or a complete system.

Fee Simple: An estate of real property that the owner has unrestricted powers to dispose of and which can be left by will or inherited. Commonly used as a synonym for ownership.

First Generation Space: Generally refers to new space that is currently available for lease and has never before been occupied by a tenant. Can also indicate the space has never been finished out.

Second Generation – would be a use that comes into play after the tenant in the first generation moves out. Such as a large retail first generation user closes and a 2nd generation user comes in to use the space for a different use in whole or in part. A large retail space may have to be redeveloped to several smaller uses in order to use all of the SF available. As shopping trends change from big box – many spaces are being transformed to other uses and divided up to several tenants to occupy the large space.

First Mortgage: The senior mortgage which, by reason of its position, has priority over all junior encumbrances – or 2nd / 3rd liens or loans. The holder of the first or senior mortgage has a priority right to payment in the event of default.

First Right of Refusal / Right of First Refusal: (Purchase) A lease clause giving a tenant the first opportunity to buy a property at the same price and on the same terms and conditions as those contained in a 3rd party offer that the owner has expressed a willingness to accept. Can include a time limitation.

First Right of Refusal / Right of First Refusal: (Lease) A lease clause giving a tenant the first opportunity to lease additional space that might become available in a property at the same price and on the same terms and conditions as those contained in a third party offer that the owner has expressed a willingness to accept. This right is often restricted to specific areas of the building such as adjacent suites or other suites on the same floor. Can include a time limitation.

Fixed Costs: Costs, such as rent, which do not fluctuate in proportion to the level of sales or production.

Fixed Expenses: Operating costs that usually do not change as a result of occupancy such as property taxes, insurance and some forms of building maintenance.

Fixed Rate Mortgage: A loan that fixes the interest rate at a prescribed rate for the duration of the loan.

FF&E: Furniture, Fixtures & Equipment: Term used to denote a list of any and all "FF&E" that the seller is offering to convey to a buyer or tenant as part of a transaction. If a sale – a "Bill of Sale" might be appropriate. Such a list should typically be fairly detailed and when / where appropriate should stipulate conditions and if Seller / Landlord is offering any sort of warranty or guarantee or maintenance after the closing of the sale – or the execution of the lease or else a buyer or tenant may find a problem / discrepancy with the FF&E and expect the Seller / Landlord to be responsible for same.

Flat Lease: A lease in which payments are made at set intervals in equal amounts throughout the life of the loan.

FLEX: A flex building is designated to be versatile and may be used for office, research and development and/or retail sales as well as manufacturing, warehousing and distributing. A typical flex building will be one or two stories tall with at least half of the rentable space used for offices (and/or retail). Ceiling heights are typically 16 feet or less. Most flex buildings also include some type of overhead door.

Floor Area Ratio (FAR): The ratio of the gross SF of a building to the land on which it is situated. Calculated by dividing the total SF in the building by the SF of land area.

Force Majeure: A force that cannot be controlled by the parties to a contract and prevents said parties from complying with the provisions of the contract. This includes acts of God such as a flood or a hurricane or, acts of man such as a strike, fire or war.

Foreclosure: A procedure by which the mortgagee (lender) either takes title to or forces the sale of the mortgagor's (borrower) property in satisfaction of a debt.

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Free Rent: A concession granted by a landlord to a tenant whereby the tenant is excused from paying rent for a stated period during the lease term.

Full Service Lease: A lease in which the stated rent includes the operating expenses and taxes for the building. Same as Gross Lease. Opposite of Net Lease. Tenant may still be held liable for any increases in operating expenses over a base year amount if so specified and agreed upon.

Full Service Rent: An all-inclusive rental rate that includes operating expenses and real estate taxes. Can be for the first year or more or for the full term of the lease. The tenant is generally still responsible for any increase in operating expenses over the base year amount.

Full Service Gross: Full Service Gross - Landlord typically covers all base year expenses. A lease under which the tenant pays a fixed amount of rent and the owner pays all the other operational expenses related to the leased space and property including utilities. Generally for office space. May or may not include janitorial services for interior office areas.

General Contractor: The prime contractor who contracts for the construction of an entire building or project, rather than just a portion of the work. The GC hires subcontractors, coordinates all work and is responsible for payment to subcontractors.

Grade Level: A term generally reflective of an overhead door that is at grade or ground level.

Graduated Rental Lease:

A lease in which rent graduates (usually increases) periodically during a lease term based on changes specified in the lease. Also called step-up lease.

Graduated Payment Mortgage:

Any loan where the borrower pays a portion of the interest due each month during the first few years of the loan. The payment increases gradually during the first few years to the amount necessary to fully amortize the loan during its life.

Grant: To bestow or transfer an interest in real property by deed or other instrument; either the fee or a lesser interest, such as an easement.

Grantee: One to whom a grant is made.

Grantor: The person making the grant.

Grace Period: Allows the parties a period of time in which to comply with the terms of the lease. This clause may specify the period of time in which the tenant must correct or "cure" a default in the rent.

Gray Box/Shell: A term that generally refers to a commercial lease space that basically offers four exterior walls and an entry door and no other tenant improvements. Tenant and Landlord negotiate to finish out to suit the interior of the space to include interior walls, floor covering, HVAC, plumbing, electric service, lights, etc. (See White (Vanilla) Box)

Gross Absorption: A measure of the total SF leased over a specified period of time with no consideration given to space vacated in the same geographic area during the same time period.

Gross: Landlord covers roof and structure, taxes, insurance and common areas. Tenant covers janitorial, utilities and outside trash removal. Increases over base year are passed through to tenant.

Gross Building Area: The total floor area of the building measuring from the outer surface of exterior walls and windows and including all vertical penetrations (e.g. elevator shafts, etc.) and basement space.

Gross Lease: A lease of property whereby the Lessor is responsible for paying all property expenses, such as taxes, insurance, utilities and repairs. There can be a "modified" gross lease where there is an exception to the lessor paying for all of the previously mentioned items. Gross leases can also include provisions for expense increase pass-through provisions. See Expense Stop / Net Lease Note: A Gross Lease is also typically referred to as a Fixed, Flat or Full-Service Lease. It is most typically used for Office, Industrial and most apartment leases. Gross lease rental rates are typically higher than NNN lease rates as the Lessor is agreeing to pay for the "NNN" as part of the base rent and is therefore not able to make adjustments and pass on any increases that might normally be able to be passed on in typical NNN leases.

Modified Gross Lease Or Gross Plus In a gross plus situation, the tenant typically pays a base rent plus a concession for utilities or expenses (typically quoted as $/square foot). The key difference between this and a net lease is the fact that the "plus" is typically fixed. This is fairly standard for many of our office buildings.

Gross Rent Multiplier:

The GRM is an easy rule of thumb to forecast a value. Gross rent is the total rental income you could realize from a building if it were 100% leased. To calculate the GRM, divide the gross rent into the sale price. If your projected monthly rental income is $15,000 and your sale price is $175,000, your GRM is $175,000 / $15,000 = 11.667. You can also make this calculation using net income, which is total possible rental income less vacancies.

GRM The computation is simple: You just divide the property's selling price by its annual gross rent. For example, if an apartment building with gross rents of $80,000 sold for $480,000 the gross rent multiplier would be 6.0. So if the rental property you're interested in has an income of say $100,000 you could figure a ball park fair market value of $600,000 (gross income x gross rent multiplier).

Gross Up: An adjustment made to operating expenses to account for the occupancy level in a building. When operating expenses are "grossed up", it means that the building's variable expenses have been adjusted upwards to the level that those expenses would be incurred if the building was fully occupied (typically 95%).

Ground Lease: A lease for the sole use / occupancy of land only. Often times - this might be for an extended period of time - up to 99 years in some cases - to allow for commercial development and amortization of the leasehold improvements. The improvements belong to the tenant. Typically used in an area that has a shortage of highly desirable land.

Ground Rent: Rent paid to the owner for use of land, normally on which to build a building. Generally the arrangement is that of a long-term lease (e.g. 99 years) with the lessor retaining title to the land.

Guarantor: One who makes a guaranty.

Guaranty: Agreement whereby the guarantor undertakes collaterally to assure satisfaction of the debt of another or perform the obligation of another if and when the debtor fails to do so. Differs from a surety agreement in that there is a separate and distinct contract rather than a joint undertaking with the principal.

Hard Cost: The cost of actually constructing the improvements (i.e. construction costs)

Hard Money Loan: A **hard money loan** is a specific type of asset-based loan financing through which a borrower receives funds secured by real property. Hard money loans are typically issued by private investors or companies. Interest rates are typically higher than conventional commercial or residential property loans because of the higher risk taken by the lender. Most hard money loans are used for projects lasting from a few months to a few years. Hard money is similar to a bridge loan, which usually has similar criteria for lending as well as cost to the borrowers. The primary difference is that a bridge loan often refers to a commercial property or investment property that may be in transition and does not yet qualify for traditional financing, whereas hard money often refers to not only an asset-based loan with a high interest rate, but possibly a distressed financial situation, such as arrears on the existing mortgage, or where bankruptcy and foreclosure proceedings are occurring.

The qualifying criteria for a hard money loan varies widely by lender and loan purpose. Credit scores, income and other conventional lending criteria may be analyzed. However, most hard money lenders primarily qualify a loan amount based on the value of the real estate being collateralized. Typically, the biggest loan one can expect would be between 65% and 75% of the property value. That is, if the property is worth $100,000, the lender would advance $65,000 - $70,000 against it. This low LTV (loan to value) provides added security for the lender, in case the borrower does not pay and they have to foreclose on the property.

http://en.wikipedia.org/wiki/Hard_money_loan

Highest and Best Use: The use of land or buildings which will bring the greatest economic return over a given time which is physically possible, appropriately supported, financially feasible.

High Rise: In the Central Business District, this could mean a building higher than 25 stories above ground level but in suburban sub-markets, it generally refers to buildings higher than 7 or 8 stores.

Hold Over Tenant: A tenant retaining possession of the leased premises after the expiration of a lease.

Hotelling: An alternative workspace concept where rather than having an assigned exclusive workspace, an employee accesses one space, perhaps being one of many such spaces in common with others on an as needed basis, and otherwise works outside of the office.

HVAC: Heating, Ventilation, Air Conditioning. A general term encompassing any system designed to heat and cool a building in its entirety, as opposed to a space heater.

Hybrid Leases: Hybrid leases mix the features of Gross, Modified Gross leases and Net leases. In these, some expenses are passed on 100% to the tenants while others are included in the rent on a gross or modified gross basis. For example, utilities and cleaning may be charged to the tenants on a Net basis (fully charged to the tenant), while operating expenses and taxes are handled on a Modified Gross basis (base amount included in the rent, with a pass-through of increases).

ICSC: Trade organization – International Council of Shopping Centers – solely for those who deal in shopping centers – leasing, management, development, construction, etc.

Improvements: In the context of leasing, the term typically refers to the improvements made to or inside a building but may include any permanent structure or other development, such as a street, sidewalks, utilities, etc.

Industrial. Industrial space is usually in buildings / areas zoned for industrial uses.

Industrial Gross: A lease with the understanding that the tenant must perform its own building maintenance, do its own repairs and pay the building utilities.

Internal Rate of Return (IRR):

Often used in capital budgeting, it's the interest rate that makes net present value of all cash flow equal zero.

Internal rate of return (or IRR) on an investment – expressed as an annual percentage – is the rate of return that makes the net present value of all cash flows (both positive and negative) from a particular investment equal to zero.

To be more specific, internal rate of return is the rate at which all future cash flows are discounted so that the present value all future positive cash flows from the investment are exactly equal to the present value of the negative cash flows (costs) of the investment.

In other words, IRR establishes the rate that all future incomes must be discounted so that the present value of all those future incomes exactly equal the amount of money initially invested.

Though only one of many approaches used to make real estate investment decisions, IRR is one of the more popular rates of return real estate investors use to measure rental property profitability because it calculates for time value of money – thereby allowing real estate investors to consider both the timing and the scale of those cash flows.

As a result, the investor can determine by IRR the rate of return to expect on his or her capital investment based upon anticipated future income streams.

Insurance and Liability:

Specifies who is responsible for casualty and liability insurance and the coverage required.

Inventory: The total amount of rentable SF of existing and any forthcoming space (whether it be a tenant vacating space or new building coming on the market), in a given category, for example, all WHS space in a specified submarket. Inventory refers to all space within a certain proscribed market without regard to its availability or condition, and categories can include all types of leased space such as office, flex, retail and WHS space.

IRS – 1099: The IRS form for the annual reporting of dividend and interest payments and rental income made to the owners / investors of the account. The total amount of rents received would be reported as income to the property owner. He / she would then offset the income by the related expenses of ownership.

Judgment: The final decision of a court resolving a dispute and determining the rights and obligations of the parties. Money judgments, when recorded, become a lien on real property of the defendant.

Judgment Lien: An encumbrance that arises by law when a judgment for the recovery of money attaches to the debtor's real estate.

Kick-Out: A term in commercial real estate leases that could outline the terms of agreement between the Landlord and the Tenant whereby specifics are set forth should an agreement be reached to enable a Tenant to opt out / terminate a lease prior to the end of the natural term agreed upon. The terms of such an agreement could call for the Tenant to reimburse the Landlord for unamortized improvements and/or unearned real estate lease commissions for the balance of the term of the lease and any other terms under which the parties can agree to enable the early termination of the lease.

Land – Size: To determine the size of a piece / parcel of land – you can use one of several sources of information: These include a survey, tax data, title report and to some extent a variety of online sources – varies to the area.

Landlord and Tenant (lessor and lessee):

Identifies the parties by their full legal names, states of incorporation, and principal business addresses.

Landlord Improvements:

Specifies which improvements the landlord is to make to the premises prior to the tenant's taking possession of the property.

Landlord's Solvency:

Specifies tenant's rights if the landlord is in financial trouble and there is a foreclosure on the leased property.

Lease: A written contract between a building owner and a tenant transferring the right to occupy a specific property and setting forth the rights of both parties to a particular property or space within a property and specifying such as rental amount, terms, conditions, etc.

Lease Types: There are several variations of types of leases – here are the most common in the industry:

Gross Lease: The tenant pays a set sum or "gross" amount for rent and the landlord pays all real estate expenses.

Net Lease: Generally a lease in which the tenant pays for utilities, and property taxes in addition to rent or insurance. The landlord pays for maintenance, repairs, and the property taxes or insurance not paid by the tenant. Also referred to as a single net lease or modified gross lease.

NN (**Net Net Lease**): Generally a lease in which the tenant pays for utilities, property taxes, and insurance in addition to the rent, and the landlord pays for maintenance and repairs. Also referred to as a double net lease, NN and modified gross lease.

NNN (**Net Net Net Lease**): A net lease under which the lessee assumes all expenses of operating a property, including both fixed and variable expenses and any common area maintenance that might apply. However, the landlord is responsible for structural repairs. Referred to as a triple net lease or NNN and stated as a fully net lease.

Absolute NNN/Bonded Lease: No landlord responsibilities. Tenant is responsible for taxes, insurance, maintenance (including roof & structure).

Absolute Net Lease: A lease in which the tenant pays all expenses including structural maintenance repairs; usually a long-term lease to a credit tenant.

Absolute Net Bond Lease: Tenant is responsible for all expenses, including casualty and condemnation.

There are several ways participants in the industry state lease terms. Some are correct, some are incorrect and some terms have the same meaning. Gross leases and modified gross leases associated with commercial real estate involve greater landlord responsibilities. Many investors focus on acquiring properties that have **Triple Net (NNN)** characteristics with creditworthy tenants.

Lease Interest: A property interest that arises from the association of a lease with a property e. g., a leased fee estate or leasehold estate.

Lease Term: The specific period of time in which the Landlord grants to the tenant the right to possession of real estate.

Leasehold: The interest or estate on which a lessee (tenant) of real estate has a lease. A long term lease in this case could be used as collateral.

Leasehold Estate: An ownership interest in real estate held by a tenant during the term of a lease. The tenant is given the right to use and occupy a property for a time and based on the restrictions contained in the lease.

Lease Purchase Agreement: Buyer makes a deposit for future purchase of a property with the right to lease property in the interim.

Lease with Option to Purchase:

A lease that gives the lessee the right to purchase the property at an agreed upon price under certain conditions at a later point in time. Note: Due to many variances involving such - TREC does not recognize these and does not provide a form. The terms of such an agreement would need to be worked out by attorneys. As licensed agents - if we were to draft such an agreement - it would be practicing law - which we can’t do as we’d be in violation of TREC Rules/Regs.

Lease Rollover: The re-leasing of a space with the same tenant, after the expiration of a previous lease on the same space.

Leasehold Improvements:

Improvements or additions made to a leased property by the lessee.

Lessee (Tenant): The party to whom a lease (the right to possession) is given in return for a consideration (rent).

Lessor (Landlord): The party (usually the owner) who gives the lease (right to possession) in return for a consideration (rent).

Letter of Intent: LOI: Sale or Lease

There are potentially multiple uses of this term. Generally a written statement that two parties to a prospective transaction (buyer/seller or lessor/lessee) intend to proceed to a final agreement in good faith on stated principal business terms of the deal to be entered into. This meaning applies when executed by both parties. Alternatively such a document may be signed only by one party and is then an indication of a willingness to enter into agreement on the stated terms and conditions. To avoid legal issues regarding offer and acceptance and thus formation of a binding contract, care should be taken to include a clause stating that there is not a specific offer and no intent to be a legally binding obligation. However, an obligation to continue to negotiate in good faith to conclusion can be created.

LLC: **Limited Liability Co.**

Load Factor: In a lease, the load factor is the multiplier to a tenant's useable space that accounts for the tenant's proportionate share of the common area (restrooms, elevator lobby, mechanical rooms, etc.). The load factor is usually expressed as a percentage and ranges from a low of 5% for a full tenant to as high as 15% for a multi-tenant floor. Subtracting one (1) from the quotient of the rentable area divided by the useable area yields the Load Factor. At times confused with the "loss factor" which is the total rentable are of the full floor less the useable area divided by the rentable area. (If a full floor broken up into multiple tenancies has a useable area of 18,000 . and a rentable area of 20,000 SF., the load factor is 11.1% and the loss factor is 10%.

Loan Contingency: A period of time used to secure financing.

LTV: **Loan To Value** – the ratio between the amount of debt on a property and that property's value.

Maintenance and Repairs:

Specifies which party is responsible for the maintenance and repair of which portions of the property

Master Lease: The dominant lease in a building or development that contains a sublease.

Master Lessor: Property Owner

Maximum Purchase Price Calculation:

It is always helpful to know the maximum price you can afford to pay when you decide to purchase real estate because it filters the search and saves you the time of looking at properties that you aren't going to purchase.

To make the maximum purchase price calculation we'll use three criteria: the amount of your cash down payment, your desired monthly mortgage payment, and the interest rate and terms for the mortgage you most likely can obtain.

Mezzanine Debt: Mezzanine debt is when a hybrid debt issue is subordinated to another debt issue from the same issuer. Mezzanine debt has embedded equity instruments (usually warrants) attached, which increase the value of the subordinated debt and allow for greater flexibility when dealing with bondholders. Mezzanine debt is frequently associated with acquisitions and buyouts, where it may be used to prioritize new owners ahead of existing owners in case of bankruptcy.

Modified Gross Leases:

This is a lease in which the rent includes building expenses like a Gross lease, but the landlord recaptures expense increases after the base year via a pass-through provision such as an operating expense, tax, or utility escalation. Some landlords use substitute escalation provisions, such as Porters' Wage escalations (NYC only) and CPI escalations. Modified Gross leases are most commonly found in multi-tenant office environments. Tenant maintenance obligations may vary greatly.

Modified Net: Typically – of the 3 NNN – taxes / maintenance / insurance – one or two of the three Ns are included in the base rent. This would be identified and specified as to which is / is not included.

Mortgage: A legal document that pledges a property to the lender as security for payment of a debt.

Mortgage Insurance Premium: The amount paid by a mortgagor for mortgage insurance. This insurance protects the investor from possible loss in the event of a borrower's default on a loan.

Mortgage Release Price:

A specific amount of money that must be paid to a lender so that the lien specified by the mortgage on a particular property will be released.

NAR: National Association of REALTORS – a professional trade organization for those involved in the real estate sales and leasing business. www.realtor.org.

NER: **Net Effective Rent** - Since commercial leases have so many nuances like free rental periods, escalations and sliding scale brokers commissions, net effective rent or NER is a way to calculate what the actual monthly costs would be when all of the variations are averaged in. But, just like anything in math, details matter. You see, there are different ways to calculate NER and the most common, known as broker's net effective rent, doesn't factor in one of the most important parts of any financial calculation: the cost of capital

NNN: **Triple Net -** Terms in commercial leases meaning: Taxes, Maintenance, Insurance; Typically in a NNN lease (see below) the tenant pays for – in whole or in part (pro-rated) any and all costs associated with that property. Taxes, Maintenance, Insurance, Repairs, Management fees, etc. – Variations shown below can be for N, NN or NNN with any 1, 2 or 3 of the Ns included. Typical also would be for the tenant to pay for individually metered utilities. Any common utilities would be included in the "maintenance" or common area (CAM) expenses. Common area maintenance is included in the NNN. Typically – landlord is responsible for such as Roof, Foundation, Walls and such is generally spelled out in a commercial lease.

Net: Typically / generally - landlord covers roof and structure, taxes and insurance. Tenant covers utilities, janitorial and common areas.

Net and Gross Leases:

Net and Gross refer to whether the base rent includes operating costs. When a lease is Net, it means that the base rent being paid does not include building taxes, insurance, utilities or other operating expenses. These must be paid for separately by the tenant. On the other hand, when a lease is a Gross lease, the tenant pays a lump sum each month, and all of these additional costs are included in the rent.

The terms Net and Gross are often incorrectly used to refer to who performs building services. This is because in many Net leases, the tenant performs its own building services. For example, it is common to see space referred to as "Industrial NNN" with the understanding that the tenant must perform its own building maintenance, do its own repairs and pay the building taxes and utilities. But it is also common to find a multi-tenant office building in which the landlord performs building services and then passes 100% of the costs onto the tenants. This is a Net lease too.

Net Lease: A lease whereby, in addition to the rent stipulated, the lessee pays such expenses as taxes, insurance and maintenance. Net/Net/Net = Taxes / Insurance / Utilities & Repairs/Maintenance. There can be Net or Net-Net or Net-Net-Net leases. The term Net Lease applies to any and all leases under which a tenant pays a portion of the operating expenses. The base rent is considerably less than that for a full service lease due to the expenses that the tenant will be responsible for on an on-going basis. Commonly used for office and industrial properties.

Net-Net-Net Lease: A lease in which the tenant pays all the operating expenses including taxes, insurance and repairs/maintenance. NNN or Triple Net leases are sometimes also called Full Net Leases. Generally the NNN expenses will be estimated perhaps based on prior experience and the total annual amount will be divided into monthly installments based on the SF the tenant occupies and collected monthly along with the rent. After the end of the year - the owner will be responsible for providing a statement of income / expense for the NNN expenses and an adjustment may be in order based on actual experience.

Net Leases: A lease in which there is a provision for the tenant to pay, in addition to rent, certain costs associated with the operation of the property. These costs may include property taxes, insurance, repairs, utilities and maintenance.

*** DOUBLE NET LEASE:** Tenant pays property taxes and insurance.

*** TRIPLE NET LEASE**: Tenant pays property taxes, insurance and common area maintenance.

*** QUADRUPLE NET LEASE**:

Tenant pays property taxes, insurance, common area maintenance and all utilities.

NOI – Net Operating Income: The operating income after operating expenses have been deducted but prior to income taxes, interest, mortgage payments being deducted. If the number is positive it is referred to as Net Operating Income or NOI, if it is a negative figure – it is referred to as Net Operating Loss or NOL.

NPV - Net Present Value: An approach used in capital budgeting where the present value of inflow is subtracted from the present value of cash outflows.

Net present value (NPV) is a return routinely used by real estate investors during a real estate analysis to gauge the profitability of a real estate investment because it does account for time value of money. That is, it accounts for the present value of future receipts anticipated from the investment. Best calculated with such as an HP 12 or HP 10 B or other business calculator.

Definition

Net present value is the difference – expressed as a dollar amount – between the present value of all future cash flows discounted at the desired rate of return and the amount of cash investment.

Formula

$$\text{NPV} = \sum_{i=1}^{n} \frac{values_i}{(1+rate)^i}$$

Example

You want a 6% rate of return to invest $100,000 for a property projecting annual cash flows of 2,000, 2,100, 2,200, 2,300, 2,400, plus cash proceeds of 130,000 anticipated from a future sale. You want to calculate the net present value in order to know whether this real estate investment will meet your goal.

To make the NPV calculation you will need a financial calculator like HB10B because it is not something you can calculate in your head. For this illustration, however, we want to show you a much easier way using our iCalculator solution.

Instructions:

1. Enter your desired rate of return as a number (i.e., 1,2,3, etc) that represents your desired rate of return a percentage.

2. Enter the dollar amount of your cash investment as a number.

3. Enter each of the cash flows you project might be collected from the rental property at the end of each year beginning with year one (CF1) through year ten (CF10). In cases where the cash flow might be a negative add the minus (-) sign. Our example includes five positive cash flows.

4. Enter the dollar amount you anticipate might be collected as cash proceeds resulting from a future sale.

5. Click the calculate button to solve the net present value

6. **Illustration**

NPV Calculator

Solves the net present value for a series of future cash flows (includes the form

RATES

Desired return*	6

CASH FLOWS

CF0 (cash investment)*	100000
CF1*	2000
CF2	2100
CF3	2200
CF4	2300
CF5	2400
CF6	
CF7	
CF8	
CF9	
CF10	

FUTURE SALE

Cash proceeds (blank = 0)	130000

*Required

SOLUTION:

NPV

Future cash flows	141,000
Present value @ 6 %:	106,362
- Initial cash investment	100,000
Result:	**$6,362**

Close comment

"Zero - Your desired rate of return goal was achieved exactly."
"Positive - You exceeded your goal."
"Negative - You failed to reach your goal."

"Your goal was met"

FORMULA:

Net Present Value = Present Value of Future Cash Flows - Initial Cash Investment

= 106,362 - 100,000 = 6,362

Source: iCalculator by ProAPOD Real Estate Investment Software

Result:

According to the net present value we calculated based upon the projected cash flows given for the rental property in our example, your desired rate of return of 6% was exceeded.

Note: A written promise to pay a certain amount of money.

Occupancy Date: Unless specifically stated otherwise in the lease, it is the date on which the tenant takes possession of its leased premises. Thus the tenant commences to occupy the space legally based on the terms of a written lease agreement. Occupancy date, possession, lease commencement typically will be the same date. Rent commencement date may be different and may involve a period of time for free or abated rent to offset the need for tenant to make repairs, do maintenance, tenant improvements, etc. and then start paying rent, hence, rent commencement date. (See Rent Commencement and Commencement Date.)

Office Space: Is loosely classified based on the quality of construction, features and the status of location:

Class A. Most prestigious buildings competing for premier office users with rents above average for the area. Buildings have high quality standard finishes, state of the art systems, exceptional accessibility and a definite market presence.

Class B. Buildings competing for a wide range of users with rents in the average range for the area. Building finishes are fair to good for the area and systems are adequate, but the building cannot compete with Class A at the same price.

Class C. Buildings competing for tenants requiring functional space at rents below the area average.

Operating Expense: The actual costs associated with operating a property such as maintenance, repairs, management, utilities, taxes and insurance. A landlord's definition of operating expenses is likely to be quite broad, covering most aspects of operating the building.

Option to Renew: A tenant's right to extend or renew a lease at certain negotiated points

Option to Purchase: A tenant's right to purchase a property at pre-negotiated points in time.

Originating Fee: A fee paid to a lender for services provided when granting a loan, usually a percentage of the face amount of the loan.

Pad Building: Pad sites are frequently found in locations in front of such as a Wal-Mart or Sam's or Costco and are sold/leased/developed to such as fast food restaurants, typically with drive-through windows. These would be absolute NNN leases. The pad site can be sold – or leased long term and would include provisions for REA – Reciprocal Easement Agreement – for visitors to access the buildings/pad sites from other approaches within the confines of the larger property. They would also have to comply with the larger property's common area agreement for maintenance.

Parking Ratio: Typically quoted in a form such as 4/1. This would mean the parking ratio for the property is 4 parking spaces per 1,000 SF. The parking ratio will vary from property type to property type and from tenant type to tenant type with some tenants requiring more of a parking ratio due to the type of tenant and type of visitors they get. A doctor's office would require a higher parking ratio as they tend to have several patients in the waiting room and several in the exam room so the need for parking is greater.

Total rentable square footage of a property divided by the number of parking spaces; typically expressed as a ratio of spaces per 1,000 square feet. As an example calculation, a 40,000 SF office building with 180 parking spaces has a parking ratio of 4.5 spaces per 1,000 SF. Different property types or tenant uses may require different parking ratios.

Pass Throughs: Refers to the tenant's pro-rata share of operating expenses (ie: taxes, utilities, repairs) paid in addition to the base rent.

Percentage Lease: Under the terms of a percentage lease, rent is based on a percentage of gross sales generated on the leased site (retail tenants). The percentage charged takes various forms:

* Straight percentage, with no minimum amount
* Minimum plus percentage
* Minimum or percentage, whichever is greater
* Minimum plus percentage, with a ceiling on the total amount

Plus E: E = Electricity - In whatever type of lease - the tenant is responsible for their own electricity expense.

Plus U: Plus utilities - may include electric, water, gas, etc. typically individually metered to the property or particular space.

Prelim: A preliminary title report that outlines matters of record relative to a property….loans, encumbrances, liens, easements, suits, claims, etc.

Present Value: The analysis of real estate investment requires an understanding of the time value of money. The idea is that inflation erodes purchasing power over time so its probable that the money an investor might collect from a real estate investment – say in three years – will not be able to purchase the same amount of goods and services as it would today.

As a result, investments in real estate are studied from a time value of money standpoint because investors understand that it is equally as important (if not more important) to determine the timing of receipts from the investment as the amount received. This is where the concept of present value comes in.

Private Mortgage Insurance: PMI – see Mortgage Insurance Premium

Procuring Cause: The proximate cause; the cause originating a series of events which, without break in their continuity, result in the accomplishment of the prime object.

Property: Gives a full description of the property being leased. This description should include the suite number, street address, city, state, and zip code. It should also include the number of square feet in the space.

Proprietary Lease: In a multi-unit building, the lease a corporation provides to the stockholders which allows them to use a specific unit under the conditions specified.

Purchase option: Gives the tenant an option to purchase the facility at the end of the lease term. This provision should specify not only the option price but also when and how the option must be exercised.

QUADRUPLE NET LEASE:

Tenant pays property taxes, insurance, common area maintenance and all utilities.

RADIUS CLAUSE: A clause in a lease whereby a tenant would be prohibited from moving and opening another store within a certain distance of the current location.

RCA: REALTORS Commercial Alliance - a division of the NAR denoting a REALTOR practices commercial real estate.

REA: Reciprocal easement agreement – comes into play with pad sites that are sold or leased in front of large retailers (Wal-Mart, Sam's, Costco, Target, etc.) that would contain limitations as to size, height, appearance, use, location, number of pads, etc. as the large retailer would not want to restrict their visibility.

REIT: Real Estate Investment Trust – a means of ownership of real estate.

Rent: States the amount of rent and when and how the rent is to be paid. In this clause, the manner in which the rent is computed should be stated, e.g., flat rent, net-rent, percentage rent, etc.

Rent Commencement: The date on which a tenant begins payment of rent. This is may be but not always be the day the tenant takes possession of the leased space, which usually occurs upon substantial completion of the tenant improvements. (See Occupancy Date). The commencement date and date of possession can be the same in the event the tenant is to perform the desired repairs, maintenance, improvements, etc. and in turn may receive a period of "free" rent or rental abatement. In that case – Possession and Lease Commencement are one and the same. After the free rent period comes the Rent Commencement date which is the date called for in the lease for the tenant to commencement payment of rent. In some cases the tenant may have already paid the actual first month's rent even though it may be for a period that is several months after Possession or Lease Commencement. In that case – the tenant's next obligation to pay rent is the month thereafter.

Renewal option: States whether the tenant has the option to renew the lease when it expires, the term of the option, and the amount of rent to be paid during the renewal term.

Revaluation Lease: A lease in which rent is adjusted periodically according to the revaluation of the real estate.

Right of entry: Gives the landlord the right to enter the premises on an as-needed basis.

RLI: REALTORS Land Institute - a trade organization for those specializing in land – sales and development.

ROFO: Right of First Offer: The right of a tenant to make an offer to purchase a property if the owner decides to put the property on the market for sale.

KW Commercial – Commercial RE Terms

ROFR: Right of First Refusal: A right granted to a party – can be either a lease property or a property for sale – whereby the holder of the ROFR would be advised of an offer from a 3rd party to purchase a property – or to lease a property (or space therein) once an acceptable price is received by the owner from the 3rd party. The holder of the ROFR would then be notified to exercise his right or to pass and typically there would be a time requirement to respond – 3 – 10 days or whatever is agreed upon.

RPA: Real Property Administrator – a designation from BOMA

RPR: REALTOR'S Property Resource. A program for REALTORS ONLY both Residential as well as Commercial that can be accessed by going to: www.narrpr.com The site offers information on millions of pieces of property in the US (virtually EVERY piece of property existing) as pulled from sources such as tax rolls and MLS systems. Free to REALTORS. An excellent tool that can be used to gather information to help in the analysis of real estate in a given area.

Sale-Leaseback: A financing technique by which the owner sells a property to an investor and subsequently rents it from the buyer for continued use. Serves to free up the capital that the original owner has invested in the property.

Second Generation Space: Space that has previously been finished out for a prior tenant. Depending on length of tenancy, use, etc. space may be in various conditions and configurations that could be suitable for lease to a new tenant with minor to major remodeling required to suit new tenant needs. See also First Generation for more info.

Second Mortgage / Second Deed of Trust / Junior Mortgage / Junior Lien: An additional loan imposed on a property with a first mortgage. Generally a higher interest rate and shorter term than a first mortgage.

Security Deposit: States the amount of the security deposit. This provision should also state what the security deposit will be used for, where it will be held, and whether it will earn interest.

Settlement Statement (HUD 1): A financial statement rendered to the buyer and seller at the time of transfer of ownership, giving an account of all funds received or expended.

Severalty Ownership: Ownership by one person only. Sole ownership.

Shell Space: Shell space is space that has never been finished out – ie: new construction – office, retail, etc. Space would typically have slab, all 4 walls and ceiling. All improvements and finish out of the interior would have to be negotiated and installed to suit tenant.

SIOR: Society of Industrial and Office REALTORS – A trade organization for those brokers and agents catering to the needs of industrial and office properties – owners, tenants, investors, etc.

STNL: STNL – no – NOT Saturday Night Live!!! - rather – Single Tenant Net Lease Retail. A single tenant net lease retail would be along the lines of a McDonald's restaurant building, a CVS or Walgreens building and the like. A building built to suit the tenant – its sole occupant. The tenant – McDonald's, CVS, etc. frequently build the building to suit their needs and then sell the building as a STNL aka Absolute NNN investment property whereby the tenant remains in control of the property and is responsible to pay for all NNN – taxes, maintenance, insurance. The lease term typically would be for 20 + years and call for several options to renew for 5 – 10 years each. These investment buildings sell very well and the value is partly based on the AAA quality of the tenant that guarantees the lease.

Step Up Lease: A lease in which rent graduates (usually increases) periodically during a lease term based on changes specified in the lease. See Graduated lease. Also known as Stair Step lease. Helps reduce the rent rate on the front end of a lease but increases it over the term to achieve an average rent yield that is acceptable to the landlord.

Straight Lease (Flat Lease): A lease specifying a fixed amount of rent that is to be paid during the entire term of the lease, usually in monthly installments.

Sub-leasehold Estate: The property interest associated with a sublease. The value of the Sub-leasehold can be estimated as the present value of the difference between the market rent and the sublease rent.

Sub-Lease: Under the terms of a sublease, a tenant leases some portion of a premises to another tenant, while remaining liable to the landlord for the rent.

Sub-Lessor: Tenant

Sub-Lessee: Sub-Tenant

Subletting or assignment:

Gives the tenant the right to sublease or assign the property if the tenant cannot fill out the term of the lease or wants to rent part of its space to someone else. This clause will specify under what conditions the tenant can avail itself of this right. Under a sublet, the original tenant is still responsible for honoring the provisions in the lease. In an assignment, the original tenant is out of the picture and has no further liability under the lease.

Taxes: Specifies whether landlord or tenant is responsible for the property taxes.

Tenancy At Will: Agreement between landlord and tenant wherein the landlord agrees that the tenant may stay in possession of the leased space after the expiration of the lease and pay rent for the time the space is occupied until landlord or tenant elects to terminate the lease. Any and all terms of the tenancy at will are entirely negotiable between the two parties involved.

Tenancy In Common: TIC – Ownership by two or more persons who hold an undivided interest without right of survivorship. In event of the death of one owner, his / her share will pass to his/her heirs.

Tenant Improvements:

Indicates whether the tenant has the right to make improvements to the property and the extent to which the landlord will allow such improvements.

TI/Tenant Improvement Allowance:
Tenant Improvement Allowance/TI:

An amount negotiated to allow for improvements to a particular space. The improvement allowance can be given lump sum or on periodic draws until completion of the improvements. Improvements can be performed by the tenant and/or the landlord. Whatever is negotiated and agreed upon by all parties.

Termination: Imposes an obligation on the tenant to return the property in a certain condition at the end of the lease.

Termination date of lease:

Specifies the lease's ending date.

Term of the lease: Identifies in months or years the duration of the lease. It should also state when the tenant is entitled to possession.

Title Insurance: An insurance policy that protects the insured (buyer or lender) against loss arising from defects in the title.

Triple Net Lease: A net-net-net lease, where in addition to the stipulated rent, the lessee assumes payment of all operating expenses of the property and the landlord receives a net rent. This includes both fixed expenses, such as taxes and insurance, and all operating expenses, including costs of maintenance and repair. In some cases, the NNN tenant even pays the interest payments on the lessor's mortgage on the property lease.

TRIPLE NET LEASE:

Tenant pays property taxes, insurance and common area maintenance for their portion of the property.

Turnkey Lease: Under the terms of a turnkey lease, a landlord agrees to turn the premises over to the tenant in a ready to use condition based on specifics negotiated as to any maintenance, repairs or improvements.

ULI: Urban Land Institute – a trade organization. The Urban Land Institute provides leadership in the responsible use of land and in creating and sustaining thriving communities worldwide. ULI is an independent global nonprofit supported by members representing the entire spectrum of real estate development and land use disciplines. www.uli.org

Use of Premises: Specifies any restrictions on the use of the premises.

Utilities and Services:

Specifies what utilities and services each party is responsible for and the days and hours provided. Water, trash, sewer, waste water, electricity, gas, CATV, telephone, etc.

Variable Expenses: Costs, such as janitorial, that may vary within a building's occupancy and by decisions made in the management of the building (Also known as Controllable Expenses)

Vanilla Box / Shell: A vanilla shell is typically a space that would be in move-in ready or near move in ready condition. The space would typically include a ceiling, lighting, electrical outlets, three walls and a store front. Some final finishing touches may be needed to complete preparation of the space for a specific tenant. (See White Box)

Warranty: Statement by the landlord that the premises are in compliance with applicable laws.

White Box: (Vanilla) A term that generally refers to a commercial lease space with the basics in place – 4 walls – unfinished Sheetrock, finished or unfinished ceiling, limited lighting and/or floor covering, if any, limited electric service, if any; generally no HVAC or plumbing or restrooms or interior walls. Would typically appear to be "finished" from outside view with walls, windows and a door. (See also Gray Box) Landlord and Tenant negotiate for completion of the interior improvements and/or Tenant may elect to take the space "as is" and finish it to suit.

Zoning: States the zoning laws or other restrictions that apply to the facility.

Conclusion: Because of the many different variations on these lease structures, it is highly recommended that practitioners refrain from using the terms "Gross" and "Net" in lease language. (For that matter, you should not use the terms "Double-Net" or "Triple-Net" either.) These terms can have different meanings to different people, and may be understood in one area differently from another area and there is no accepted standard as to which "Net" refers to which expense. As a rule, it is always better to spell out the actual obligations of the parties.

For assistance or more information - contact your real estate professional. Make sure he / she is an experienced Commercial REALTOR.

The above collection of commercial real estate terms has been collected over many years from a variety of sources and as I come across new or previously not included terms or better examples / definitions, etc. I will update this list.

Provided for you as a courtesy by Chris Rosprim, CPM / REALTOR / Broker with KW Commercial Real Estate Services. 2434 Lillian Miller Parkway, Denton, TX 76205, 940-243-4000 / 940-453-2180; chrisrosprim@kwcommercial.com Serving your real estate needs throughout the north Texas area.

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