

CRE FINANCE COUNCIL



E-LEARNING

COMMERCIAL REAL ESTATE (CRE) 100

GLOSSARY OF TERMS



Acceleration Clause

Contract provision that allows lender to require a borrower to repay all outstanding principal if loan covenants are not met.

Amortization

A process of repaying loan principal in a series of fixed payments over a period of time until the debt is paid off; the periodic payment consists of a growing portion of principal and a declining portion of interest over time.

Bundle of Rights

A common way to explain the complexities of property ownership – how multiple parties can simultaneously hold interests in the same property, including, but not limited to the right to possess, extract, mortgage, alienate, or bequeath.

Capitalization (Cap) Rate

Defined as the net operating income (I) for the year divided by the appraised value of the property (V) [$I/V = R$]. It is used as a measure and/or benchmark for a property's value based on current performance. Cap rates also serve as an indicator of investor expectations.

Commercial Real Estate (CRE)

Property that is owned/leased for the purpose of producing income.

Crowd-Funded Ownership

The pooling of money from a group of investors to make an investment in real estate.

Debt Service Coverage Ratio (DSCR)

The ratio of a property's net operating income or net operating cash flow to the debt service payments on the loan backed by the property, calculated by dividing the NOI or NCF by total debt service. DSCR is a measure of a mortgaged property's ability to meet monthly debt service payments; higher ratios are more desirable. A DSCR less than 1.0 means that there is insufficient cash flow by the property to cover debt payments.

Deed

A legal instrument in writing which passes, affirms or confirms an interest, right, or property and that is signed, attested, delivered, and in some jurisdictions, sealed. It is commonly associated with transferring (conveyancing) title to property.

Default Risk

The possibility that something could happen during loan term that would cause the borrower not to be able to meet the obligations of the loan, such as property level income declining below the debt service required.

Discount Rate

In a discounted cash flow analysis, the rate applied to each year's cash flow from a property to determine the net present value (NPV) of a series of cash flows. Based on the periodic weighted average cost of capital or the required return for a real estate investment.

Due-On-Sale Provision

Requires the mortgage to be repaid in full upon a sale of the property to a third party.

Estoppel

Agreement provided by tenant to mortgage lender verifying the lease and certain terms.

Fee Simple Ownership

Complete form of ownership that entitles owner to full use of the property – both the land and the improvements – which is only limited by zoning laws/deed or subdivision restrictions and includes the full bundle of rights.

Floating Interest Rate

Interest rate fluctuates with the market over the duration of the loan – constructed by using a spread over an appropriate index.



General Warranty Deed

A type of deed where the grantor or the seller guarantees that he/she holds clear title to a piece of real estate and has a right to sell it. The guarantee is not limited to the time the grantor owned the property. It extends back to the property's origins.

Ground lease

A lease on land that covers the land but not improvements or buildings on that land. In other words, the land and buildings are separate entities and are separately owned. Building owner pays rent on the land via agreement known as a ground lease.

Interest Rate Risk

The danger that the value of a bond or other fixed-income investment (e.g., a mortgage) will suffer as the result of a change in interest rates. Investors can reduce interest rate risk by hedging fixed-income investments with interest rate swaps and other instruments.

Investment Value

The value of a property to a particular investor.

Lien

Legal right granted by the owner of property. It serves to guarantee an underlying obligation, such as the repayment of a loan. If the underlying obligation is not met the creditor may be able to seize the asset.

Liquidity

A measure of the ease and frequency with which assets such as CMBS are actively traded in the secondary market. Liquidity is related to issuance / trading volume; the greater the outstanding and ongoing issuance / trading of a certain asset such as CMBS, the greater the liquidity typically is (i.e., the ease of converting it to cash).

Loan Amount

Amount of principal (loaned proceeds) that the borrower promises to and is legally required to repay and is set forth in the loan documents.

Loan to Value (LTV) Ratio

The ratio of the principal amount on a mortgage to the appraised value of the collateral property. The ratio is commonly expressed to a potential borrower as the percentage of value a lending institution is willing to finance. The ratio is not fixed and varies by lending institution, the borrower's credit history, the property type, geographic location, size and other variables. The ratio will change over time as the loan balance and valuation changes and is used as a measure of risk on a secured loan (higher LTV ratios are reflective of higher risk).

Maturity Risk

The possibility that the borrower will not pay back the amount, usually called a balloon payment, due at maturity.

Mortgage

Debt instrument, secured by the collateral of specified real estate property, that the borrower is obliged to pay back with a predetermined set of payments.

Net Operating Income (NOI)

Gross operational revenues earned by a property less operating expenses but before mortgage payments, tenant improvements, replacement reserves and leasing commissions. NOI is typically used to analyze the profitability of income-generating real estate investments and as the basis for calculating debt service coverage ratios.

Operating Expenses

Costs associated with the operation and maintenance of an income-producing property. These can include: insurance premiums, legal fees, utilities, property taxes, repair costs, and janitorial fees.

Periodic Payments

Regular payments (typically monthly, but quarterly or annual also) made consisting of interest and/or interest and principal.

Present Value (PV) or Net Present Value (NPV)

Current value of a future sum of money given a specified rate of return (i.e., discount rate).



Repayment Risk

The possibility that the borrower may not repay loan at maturity.

Single Tenant Triple Net Lease (NNN)

Lease agreement on a property where the lessee (tenant) agrees to pay the net amount for following three types of costs: real estate taxes on the leased asset, building insurance, common area maintenance.

Subordination, Non-Disturbance, and Attornment Agreement (SNDA)

An agreement, often in recordable form, between tenant, lender and the borrower. An SDNA is a negotiated item and not automatic for lenders to provide.

Term Risk

The possibility that the borrower may not make periodic loan payments when due during the term of the loan.

Title Insurance

Protects real estate owners and lenders against property loss or damage from mistakes or missing information from the title due to liens, encumbrances, or defects.

Valuation

Process of developing an opinion of value, for property (usually market value).