

CLASS #1.

WHAT IS MOTIVATING YOU TO INVEST IN REAL ESTATE?

Primary residence

- What is the likelihood you will relocate within five to seven years?
- How likely will your household size change, and can the property sustain the change?
- Do you have financial resources and income stability to handle the unexpected, which should be expected?
- Does it make your heart go pitter-patter?

Part-time residence (vacation property)

- How many nights a year do you intend to occupy
- If you plan on renting to others part-time, what restrictions exist that could limit renting? (local and home ownership)
- How will you manage if you are not nearby?

Rental investment property

- Do you have the skill, time, and money necessary to manage?
- Is your personality suited to speaking with tenants, brokers, and other professionals? Can you stay calm when things go wrong?
- Will it produce a superior return to other investments (Stocks and Bonds)?
- Will it achieve diversification of your portfolio?
- Are you in a position to finance the acquisition at attractive interest rates?
- Do you have the capital to sustain repairs and vacancies?
- Will a “taxable loss,” which may arise from the depreciation deduction, be helpful to you in offsetting gains from other income?
- Have you considered capital gains tax and depreciation recapture tax when you sell?

Some thoughts Before you make the plunge

- Have you established your emergency fund?
- Do you have a unique housing situation that is less than the market rate? (rent-controlled apartment, living with family, etc.)
- Understanding LIQUIDITY: Real estate is NOT easily converted into cash; there are costs to purchase and sell, which can eat up any gain if held for a short time.
- Consider risks, such as job stability,

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11.00 Instructor’s Notes - Real Estate Segment – Outline

FINANCIAL CONSIDERATIONS

How much do you have for a down payment?

- Do you have 20% cash for the down payment? If you have less than 20%, you must purchase Private Mortgage Insurance (PMI). PMI is an ongoing cost of approximately .03% to 1.15% of the amount borrowed and will be invoiced by the Mortgage company as long as the mortgage is in place.
- Is your down payment easily accessible (liquid)?
- Are you planning on borrowing from a 401 K retirement account? (What are the repayment terms, interest, and term)
- Are you relying on a gift or loan from a family member or friend?
 - Discuss documenting the loan to protect claims from other family members.
 - Discuss the need for the funds to be in your account a few months before the mortgage application, as the mortgage company will require proof.
 - Discuss the statement you must sign declaring the funds are NOT borrowed.

Will you save money by this purchase - Compare Rental vs Home Ownership expenses

HANDOUT 11.01

Renter	\$	Home Owner	\$
Rent		Real Estate Taxes	
Insurance		Insurance	
		Home Owners Maintenance fees	
		Finance cost (principal and interest)	
		Subtotal:	
		Heat (oil or gas)	
Gas and Electric		Gas and Electric	
Phone, Internet Cable,		Phone, Internet, Cable	
		Garden Maintenance	
		Water and Sewer	
		Snow Removal	
		Repairs	
TOTAL		TOTAL	

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11.00 Instructor's Notes - Real Estate Segment – Outline

Are you an excellent candidate to take out a mortgage?

- What is your credit score? Discuss small steps to make a significant improvement.
- Bank Criteria - Historic
 - HISTORIC Criteria = Interest, Principal & RE Tax, and all required installment debt must be no more than 38% of gross income.
 - MORE LENIENT Criteria = Interest, Principal, RE Tax, and all required installment debt must be no more than 50% gross income.
- Discuss pre-qualification letters (and their worth)
- Discuss pre-approval letters
- If your income does not come from a W-2, more documentation is needed, and in general, it will be harder to qualify – need to prove net profit (Schedule C)
- Do you qualify for any special programs? i.e., veterans first-time homebuyers (generally, they relate to the amount of down payment, not the interest) - however, being an existing customer can lower your interest rate
- Discuss interest-only loans, balloon loans, 203K loans, splitting loans between primary and secondary (HELCO)

Will you save on taxes?

- Are you currently using the standard deduction or itemizing (Schedule A)? –
- Calculate two ways to see if there will be savings.
 - *Method A – STANDARD DEDUCTION Determine your “Filing Status” (Single, married filing jointly, married filing separately, head of household) and then the appropriate Standard Deduction*
 - *Method B – ITEMIZED DEDUCTION - (Schedule A)*
 - *medical expenses over 7.5% of Adjusted Gross Income (Page 1 tax return)*
 - *state and local income taxes & real estate taxes (limit is \$10,000 per year)*
 - *Primary mortgage interest (limit is \$10,000) – other restrictions apply*
 - *charitable contributions*

Which method produces a more significant deduction? Note that

- Mortgage Insurance Premium – not deductible
- Home Owners Equity line of credit – no longer deductible
- *Commercial Property (reported on Schedule E) - if the operation produces a loss (often due to depreciation expense), the loss cannot be used against other income IF you use the property more than 10% for yourself.*

THE FIRST CLASS ENDED HERE

MONEY 101 EDUCATION

11.00 Instructor's Notes - Real Estate Segment – Outline

CLASS # 2

Review of homework...rent vs. purchase

Research Properties & SHOPPING – The FUN PART.

(REVIEW HANDOUT 11.02 – Factors to consider when shopping)

- Location, Location, Location—Determine the Neighborhood where you want to invest. Choose an area close to your job and family; transportation Brokers often use a trendy name to attract buyers, which may not accurately reflect the neighborhood. Check Google map descriptions.
- Size of the unit (bedrooms, bathrooms) square footage
- Transportation issues – proximity to public transportation, parking/garage included
- Building amenities will increase Common Charges – door staff, live-in superintendent, onsite management company, laundry in building, gym, roof deck, sports facilities.
- Unit factors, layout, light, size, amenities (appliances) – Be realistic about renovations. Compare properties in terms of price per sq. ft. In NYC, size is king.
- Price – consider not only the cost of the unit but also the ongoing real estate taxes and standard charges/maintenance fees
- Prepare a chart for every home visited and follow up to determine the selling price. Use HANDOUT 11.02 Unit Information Sheet.
- The Search - See at least 25 properties within a given location to understand their values.
- What is the difference between a Cooperative and a Condominium?

Resources:

- Look initially on your own - in NYC, the primary search tool www.StreetEasy.com
- Outside of NYC, use www.Zillow.com www.FSBO.com www.realtor.com

Using a Broker

- What are the commission structures (Sellers Broker aka Listing Broker) and Buyer's Broker –
- Are rates negotiable? – When signing a commission agreement, what are the key restrictions?
- What are the contract restrictions?

Pros – a good broker will

- Pre-screen the properties, and only show you those that meet your criteria.
- know which buildings have more demanding criteria to get past a coop board
- and help find a compromise with difficulties that arise with the seller
- If the property is already listed on the MLS (Multiple Listing Service), there are no savings by the purchaser going directly to the seller.
- The seller has already entered into a contract that binds them (generally for six months) to sell only through the Listing Broker. However, if you contact the Seller's broker, you

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may ultimately be able to negotiate a small discount if there is no Buyer's broker.
(Discuss this strategy when SELLING a unit).

- When selling a unit, a good broker will recommend the repairs that should be done before listing and can advise and even arrange for vendors/handy persons. This service is vital if there are issues in the inspection.
- A good broker often recommends a closing attorney who "gets the job done."

Cons

- The broker becomes another person in the mix, which can derail communication.
- A nonresponsive broker can do a lot of harm.

Going it alone

- FSBO listings are sellers trying to avoid commissions. Often, they need better photographs of the property, and Sellers usually overvalue units.
- Finding a property on your own – look for the building, layout, floor –
- Research on who owns a unit can be done through the tax office of most cities – it does not work for cooperatives – It is generally best to have the Block and Lot information
- In NYC, use ACIRS or BIS system to look up property ownership information

Building factors - Looking under the cover – meeting the neighbors

- **Building amenities,**
 - Lobby/Front Door staff (personnel costs drive up maintenance fees),
 - height of the building (FISP is concerned if it is over six stories)
 - if you can obtain the financials (look at the reserve fund),
 - Get the meeting minutes. Is there an assessment in place
- **Building Finances –**
 - Is there a Flip Tax
 - Have there been Assessments (purpose)
 - Do shareholders owe standard charges - Accounts Receivable
 - Has the building paid its vendors = Accounts Payable
 - Are there adequate funds for an emergency Reserve Fund
 - Is the building subject to Local Law 11 – FISP
- **Building staff**
 - Are they unionized
 - Is there a full-time doorman/concierge
- **BUILDING AMENITIES AND CONCERNS**
 - Are there building violations – using the DOB database to search
 - Is there more than one elevator
 - Sublet policy – especially for cooperatives or vacation properties
 - Are Owners utilizing the property for short-term rental (Airbnb)

THE SECOND CLASS ENDED HERE

CLASS #3

BECOMING MORTGAGE READY - PAPERWORK TO GATHER IN ADVANCE

- Photo ID to prevent identity theft and mortgage fraud
- Authorization to pull a credit report (Your lender has the form; you sign it)
- **PROOF OF INCOME** Proof of income (see below for specifics) including:
 - Two years tax returns
 - Current paystubs
 - or a letter from your employer verifying income
- **PROOF OF DOWNPAYMENT**
 - **BANK STATEMENTS**—Proof of where you are getting the down payment. Usually, three months' bank statements are required, but if a contribution is being made by someone else, they WILL have to provide the same (very intrusive), but it is required due to money laundering issues.
 - **GIFT LETTER** If someone else is providing funds for a down payment, a letter indicating this is a gift, not a loan- if it is a loan, the bank will want to know the repayment terms and will factor into debt
- **PERSONAL FINANCIAL STATEMENT** - showing all assets and all liabilities and net worth – for condo and coop board review, you will need to provide proof; thus, bank statements
- **Condominium and Cooperative Boards have additional requirements – called BOARD PACKAGES; they may want to see**
 - credit card invoices,
 - Three reference letters from people who know you (helpful if one is your accountant)
 - explanation of why you want to relocate,
 - who will reside in the apartment,
 - is this a primary residence?
 - you will also need to have an INTERVIEW
- **OPTIONAL**
 - **PROOF OF RENT PAYMENT HISTORY** – A letter from a landlord can be helpful to show you are a “good paying tenant” as rent payments do not appear on a credit report.
 - Personal Letter of introduction – this can be helpful in a buying frenzy.
 - Proof (Binder) showing homeowners insurance (For a purchase, you won't need this until just before closing)

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PROFESSIONALS YOU WILL NEED

- Attorney for closing – negotiate in advance the fee, so you have time to shop
- Accountant – who has done your tax returns
- Insurance Broker – who can arrange a binder for home owner's insurance

MAKING AN OFFER – SIGNING A PURCHASE CONTRACT

Pricing

- There is nothing wrong with making a full-price offer if this is the home of your dreams, AND it represents value.
- Discuss Bidding wars, Sealed offers, Best and Final
- Write a letter to the Seller - Knowing something about you may increase your chances of success. *Brokers try to keep the parties from communicating, but sometimes, direct contact is helpful.*

Acceptance—If accepted, expect to sign the contract and give a 10% deposit within 24 hours.

Key clauses

- Price (this should not be the only focus)
- Attorney Review date (usually 3-5 days)
- Who holds the down payment in escrow? Is it in an interest-bearing account?
- Home Inspection Date (generally within two weeks)
- Cancellation Clause (3 days after attorney review)
- Mortgage Contingency Date Clause (generally 45 days – this is a big issue as it will take longer to get the commitment – discuss extensions)

What do they mean by an “all cash offer”? – the risk of losing the deposit

THE THIRD CLASS ENDS HERE

CLASS # 4

HOW MUCH OF A MORTGAGE CAN I AFFORD?

- What are the banks seeking in terms of debt-to-income ratio? *-this changes from time to time -*

- What is included in income?

Discuss two-party purchasing, alimony, dividends and interest

- What is included in debt?

ALL LIABILITIES THAT HAVE A REQUIRED MINIMUM PAYMENT, including credit card payments, student loan payments, car or installment loan payments, and FUTURE obligations once the property closes – thus the mortgage payment, PMI payment, real estate taxes, homeowner association fees, and property insurance.

Review 11.31. How large of a mortgage can I qualify for?

HOW MUCH CASH will I need to close?

- Purchase Price plus closing costs less mortgage amount = CASH NEEDED

WHAT Closing Costs should I anticipate? **Review 11.51 and 11.52**

- Title Insurance – arranged through your attorney (discuss a market rate rider vs. coverage just for the mortgage)
- Mortgage Recording Tax – often at the State AND local level
- Mansion Tax – often charged on properties valued at over 1 million
- Escrowed Real Estate Taxes- held by the bank (review an escrow statement)
- Escrowed Insurance – held by the bank
- Pre-paid Maintenance – if the seller has prepaid a month, there is a reimbursement
- Co-Op or Condo – Buy-In contribution to the Reserve Fund – expected in co-ops that try to raise money through a “flip tax” or in new developments
- Reimbursement for fuel paid by the Seller

Seller Costs:

- Real Property Transfer Tax – generally paid by the seller but not always
- Flip Tax – often charged by a cooperative (and occasionally a condominium)
- Real Estate Broker fee

REAL ESTATE CLOSING SETTLEMENT STATEMENT **Review 11.55, 11.56, 11.57**

SHOPPING FOR A MORTGAGE

Compare different bank offers – important factors:

- Term: Residential - common are 15 and 30. For residential mortgages, always get a 30-year term. While a 15-year term may offer a lower interest rate, it will result in a higher monthly payment, and life bumps may make sustaining the higher payment difficult. Commercial mortgage terms seldom go beyond 20 years.
- Origination Fee (aka points): While paying points lowers the interest, it is generally NOT a good idea as you need to know how long you will keep the mortgage.
- Interest rate – fixed or variable (understand for variable how often the rate changes, what the rate is based on (discuss prime and LIBOR), and whether there is a limit to the change (annual AND mortgage lifetime) **REVIEW 11.33 and 11.34 AMORTIZATION CHART**
- Other bank-related fees include credit checks, Bank attorney fees, recording fees, appraisal fees, and a title search fee.
- RECOMMENDATION – when comparing mortgage offers from multiple banks, compare a 30-year term 0 Point offer

Mortgage vocabulary

- Prepayment penalty
- Payoff amount
- Amortization - (review a chart) Understand the cumulative cost of interest and how little of the Principal is paid off in the first ten years
- Subordinated debt (home equity line)
- Balloon Payments

THE FOURTH CLASS ENDS HERE

CLASS # 5

INVESTMENT REAL ESTATE

Does it meet your financial diversification goals?

Financial aspects to consider

- How to fund – consider the opportunity cost
- Determining cash flow break-even
- Consider vacancies
- Turnover costs. (advertising, painting, cleaning, updating) and
- Change in rental Market Value is not linear
- Understanding Depreciation Expense – benefit
- Passive vs. Active Income
- Understanding rent roll capitalization for valuation
- Taxes due when property is sold - Understanding capital gains and Depreciation recapture tax
- 1031 exchange

Management aspects

- Professionals vs. self-managed
- Finding Tenants – broker fees
- Credit risks, screening
- Security deposit restrictions – with the change in the laws,
- Setting up electronic rent payments
- Eviction

Real Estate Investment Trusts (REIT)

Instead of owning a single property that you must manage, consider a REIT.

REITS take investors' money, purchase, and manage hundreds of properties, spreading the risk across different geographic areas. REITs have a professional management team skilled in property management. They look to profit from each building and return that profit to shareholders. REITs give investors the upside of real estate investment with fewer headaches.

- Choice DOMICILE: Domestic REITs (invest in real estate within the US) vs. International REITs (invest in real estate outside the US).
- Choice TYPE OF PROPERTY: REITs can invest in offices, apartment buildings, single-family houses, warehouses, retail centers, medical facilities, data centers, cell towers, infrastructure, and hotels. Most REITs focus on a particular property type, but some hold multiple types of properties in their portfolios.

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FROM NERD WALLET - Best-performing REIT Electronic Traded Funds (ETF)

These can be purchased through any brokerage house (i.e., Fidelity, Vanguard, Schwab), and as they are ETFs, you do not have to buy an entire share, but you can get a fraction.

Symbol	ETF name	5-year return	Expense ratio
INDS	Pacer Industrial Real Estate ETF	6.26%	0.55%
XLRE	Real Estate Select Sector SPDR Fund	3.48%	0.09%
NURE	Nuveen Short-Term REIT ETF	3.47%	0.35%
REZ	iShares Residential and Multisector Real Estate ETF	3.07%	0.48%
USRT	iShares Core U.S. REIT ETF	2.59%	0.08%

Data as of May 1, 2024. Sources: Naret, Morningstar, and VettaFi.

Nerd Wallet's Full article on REITs:

<https://www.nerdwallet.com/article/investing/reit-investing>

REVIEW OF HANDOUTS

- 11.60 Commercial Property Cash Flow
- 11.62 IRS form Schedule E – Supplemental Income and Loss
- 11.63 Evaluating a Commercial Real Estate Opportunity – at different purchase prices
- 11.65 Depreciation Expense for an Investment Property

THE FIFTH CLASS ENDS HERE