

## Investors

Are you thinking about buying an investment property? You'll need a cash investment – downpayment plus closing costs – but it will save you on taxes. The rent you charge will cover a portion of your expenses. (If you have a large enough downpayment, or the house is inexpensive enough, you may find your house paying its own expenses. You can deduct the operating expenses of the property (including the mortgage and taxes) plus depreciation. Homes tend to go up in value over time, although not at the moment, so your property may be worth more later. Rents tend to increase a few percent a year so eventually your rents will cover your operating expenses if you keep your costs under control.



## Terms You Should Know

**Cap Rate** – if you divide the income the property generates each year by the price you paid for the property, that's your cap (capitalization) rate. You want the highest cap rate you can get, but properties in very desirable locations offer lower cap rates.

**Cash Flow** – when the income from your property covers your operating expenses. When a property cash flows, you no longer put money into the property for regular operating expenses. You may still choose to spend money to improve the property.

**Cash on Cash Return** – how much cash your investment generates based on the money you invested. This is similar to return on investment (ROI) in any other business. You must achieve positive cash flow before you get any cash on cash return.

**Depreciation** – the IRS lets you deduct the cost of residential income property (the house, not the land) over 27.5 years. That's money you deduct from your income taxes, but it's not cash out of pocket. The IRS wants some of this back when you sell the property unless you do a tax-deferred exchange.

**Expenses** – the costs of running the rental property, including water and garbage, utilities, maintenance, and taxes.



**Fair Housing** – you may not discriminate against people based on their sex, race, religion, familial status, disability, age, sexual orientation, or place of origin. Talk about your property, and the neighborhood, not about the tenants you want.

**Gross Rent Multiplier** – multiply the monthly rent by a number you're comfortable with and set that as the maximum price you'd be willing to pay for the property.

**Net Operating Income** – the money you earn after expenses, before you make your mortgage payments.

**Potential Rental Income** – what you'd earn if the property was 100% rented at all times, pretty much an impossibility. Deduct 5% from this number to get a more realistic gross income.

**Tax-Deferred Exchange** – you may be able to defer capital gains and depreciation recapture taxes if you purchase another property costing more than the one you're selling within a defined time period.

None of this is legal advice, nor am I actively working as a real estate agent.