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## Glossary of REIT Terms

### **Adjusted Funds From Operations (AFFO)**

This term refers to a computation made by analysts and investors to measure a real estate company's cash flow generated by operations. AFFO is usually calculated by subtracting from Funds from Operations (FFO) both (1) normalized recurring expenditures that are capitalized by the REIT and then amortized, but which are necessary to maintain a REIT's properties and its revenue stream (e.g., new carpeting and drapes in apartment units, leasing expenses and tenant improvement allowances) and (2) "straight-lining" of rents. This calculation also is called Cash Available for Distribution (CAD) or Funds Available for Distribution (FAD).

### **Capitalization Rate**

The capitalization rate (or "cap" rate) for a property is determined by dividing the property's net operating income by its purchase price. Generally, high cap rates indicate higher returns and greater perceived risk.

### **Cash (or Funds) Available for Distribution**

Cash (or Funds) available for distribution (CAD or FAD) is a measure of a REIT's ability to generate cash and to distribute dividends to its shareholders. In addition to subtracting from FFO normalized recurring real estate-related expenditures and other non-cash items to obtain AFFO, CAD (or FAD) is usually derived by also subtracting nonrecurring expenditures.

### **Cost of Capital**

The cost to a company, such as a REIT, of raising capital in the form of equity (common or preferred stock) or debt. The cost of equity capital generally is considered to include both the dividend rate as well as the expected equity growth either by higher dividends or growth in stock prices. The cost of debt capital is merely the interest expense on the debt incurred.

### **DownREIT**

A DownREIT is structured much like an UPREIT, but the REIT owns and operates properties other than its interest in a controlled partnership that owns and operates separate properties.

### **EBITDA**

Earnings before interest, taxes, depreciation and amortization. This measure is sometimes referred to as Net Operating Income (NOI).

### **Equitization**

The process by which the economic benefits of ownership of a tangible asset, such as real estate, are divided among numerous investors and represented in the form of publicly-traded securities.

### **Equity Market Cap**

The market value of all outstanding common stock of a company.

### **Equity REIT**

A REIT which owns, or has an "equity interest" in, rental real estate (rather than making loans secured by real estate collateral).

### **Funds From Operations (FFO)**

The most commonly accepted and reported measure of REIT operating performance. Equal to a REIT's net income, excluding gains or losses from sales of property, and adding back real estate depreciation.

### **Hybrid REIT**

A REIT that combines the investment strategies of both equity REITs and mortgage REITs.

### **Implied Equity Market Cap**

The market value of all outstanding common stock of a company plus the value of all UPREIT partnership units as if they were converted into the REIT's stock. It excludes convertible preferred stock, convertible debentures and warrants even though these securities have similar conversion features.

### **Leverage**

The amount of debt in relation to either equity capital or total capital.

### **Mortgage REIT**

A REIT that makes or owns loans and other obligations that are secured by real estate collateral.

### **Net Asset Value (NAV)**

The net "market value" of all a company's assets, including but not limited to its properties, after subtracting all its liabilities and obligations.

### **Positive Spread Investing (PSI)**

The ability to raise funds (both equity and debt) at a cost significantly less than the initial returns that can be obtained on real estate transactions.

### **Real Estate Investment Trust Act of 1960**

The federal law that authorized REITs. Its purpose was to allow small investors to pool their investments in real estate in order to get the same benefits as might be obtained by direct ownership, while also diversifying their risks and obtaining professional management.

### **Real Estate Investment Trust (REIT)**

A REIT is a company dedicated to owning, and in most cases, operating income-producing real estate, such as apartments, shopping centers, offices and warehouses. Some REITs also engage in financing real estate.

**REIT Modernization Act of 1999**

Federal tax law change whose provisions allow a REIT to own up to 100% of stock of a taxable REIT subsidiary that can provide services to REIT tenants and others. The law also changed the minimum distribution requirement from 95 percent to 90 percent of a REIT's taxable income -- consistent with the rules for REITs from 1960 to 1980.

**Securitization**

Securitization is the process of financing a pool of similar but unrelated financial assets (usually loans or other debt instruments) by issuing to investors security interests representing claims against the cash flow and other economic benefits generated by the pool of assets.

**Straight-lining**

Real estate companies such as REITs "straight line" rents because generally accepted accounting principles require it. Straight lining averages the tenant's rent payments over the life of the lease.

**Tax Reform Act of 1986**

Federal law that substantially altered the real estate investment landscape by permitting REITs not only to own, but also to operate and manage, most types of income-producing commercial properties. It also stopped real estate "tax shelters" that had attracted capital from investors based on the amount of losses that could be created.

**Total Market Cap**

The total market value of a REIT's (or other company's) outstanding common stock and indebtedness.

**Total Return**

A stock's dividend income plus capital appreciation, before taxes and commissions.

**UPREIT**

In the typical UPREIT, the partners of the Existing Partnerships and a newly-formed REIT become partners in a new partnership termed the Operating Partnership. For their respective interests in the Operating Partnership ("Units"), the partners contribute the properties from the Existing Partnership and the REIT contributes the cash proceeds from its public offering. The REIT typically is the general partner and the majority owner of the Operating Partnership Units. After a period of time (often one year), the partners may enjoy the same liquidity of the REIT shareholders by tendering their Units for either cash or REIT shares (at the option of the REIT or Operating Partnership). This conversion may result in the partners incurring the tax deferred at the UPREIT's formation. The Unitholders may tender their Units over a period of time, thereby spreading out such tax. In addition, when a partner holds the Units until death, the estate tax rules operate in a such a way as to provide that the beneficiaries may tender the Units for cash or REIT shares without paying income taxes.

*Source: National Association of Real Estate Investment Trusts, 2007.*