IMPORTANT NOTE: The National Association of REALTORS®, its faculty, agents, and employees are not engaged in rendering legal, accounting, financial, tax, or other professional services through these course materials. If legal advice or other expert assistance is required, the student should seek competent professional advice.

NATIONAL ASSOCIATION OF REALTORS®
Global Business and Alliances
430 North Michigan Avenue
Chicago, Illinois 60611
USA

Telephone: 312-329-8369
Toll-free: 800-874-6500 (U.S.)
Fax: 312-329-8358
cips@realtors.org
www.Realtor.org/global
# Contents

**Introduction** ................................................................................................................................. 1

- Course Learning Goal .................................................................................................................. 2
- Course Overview .......................................................................................................................... 2
- Learning Objectives ..................................................................................................................... 3
- Exam ............................................................................................................................................ 4
- Activities and Class Procedures .................................................................................................. 4
- Earning the CIPS Designation ....................................................................................................... 4

1. **Researching a Market at Home or Abroad** ............................................................................ 7

   - In This Chapter .......................................................................................................................... 8
   - The Country Assessment Model ............................................................................................... 9
   - Country Assessment Model ....................................................................................................... 10
   - Interpreting Country Assessment Model Data ........................................................................... 11
   - Applying the Assessment Model in Your Home Market ............................................................ 17
   - Skill Practice—Assessing Your Local Market .......................................................................... 18
   - Key Point Review ..................................................................................................................... 20

2. **The Metric World** .................................................................................................................... 23

   - In This Chapter .......................................................................................................................... 24
   - Area ........................................................................................................................................... 25
   - Dimensions ............................................................................................................................... 27
   - Land .......................................................................................................................................... 28
   - Skill Practice ............................................................................................................................. 29
   - Key Point Review ..................................................................................................................... 31

3. **Money Concepts** ..................................................................................................................... 33

   - In This Chapter .......................................................................................................................... 34
   - Small Changes = Big Impact ....................................................................................................... 35
   - Currency Fluctuation: Offer to Closing and Beyond ................................................................. 36
   - Why Currency Values Fluctuate ............................................................................................... 39
   - Managing Exchange Rate Risk ................................................................................................. 42
   - Exchange Rate Web Sites ......................................................................................................... 43
   - Using Exchange Rates to Convert Values ............................................................................... 44
4. Tax Matters ........................................................................................................... 55
   In This Chapter ................................................................................................. 56
   Taxpayer Status ............................................................................................... 57
   Tax Treaties ....................................................................................................... 58
   Substantial Presence ................................................................................------- 58
   Taxpayer Identification Number ...................................................................... 59
   Income Tax for Foreign Real Estate Owners ................................................... 60
   Taxable Income from Real Estate ..................................................................... 61
   Foreign Investment in Real Property Tax Act (FIRPTA) ................................. 62
   Capital Gains Tax .............................................................................................. 65
   Estate Tax .......................................................................................................... 66
   Forms of Ownership .......................................................................................... 67
   State and Local Regulations ........................................................................... 69
   Federal Reporting Requirements ...................................................................... 69
   State Reporting Requirements ........................................................................ 71
   Key Point Review .............................................................................................. 73

5. U.S. Visas ............................................................................................................. 77
   In This Chapter ................................................................................................. 78
   Visa Waiver Program ..................................................................................... 79
   Visas for Personal and Business Travel ............................................................ 80
   Arrival in the U.S. ............................................................................................. 84
   Working in the United States .......................................................................... 85
   www.state.gov .................................................................................................. 86
   Key Point Review .............................................................................................. 87
6. Value Concepts ................................................................................................................. 91

In This Chapter ..................................................................................................................... 92
Four Investment Elements .................................................................................................. 95
Time/Value of Money .......................................................................................................... 97
Value Approaches ................................................................................................................ 100
Sales Approach ..................................................................................................................... 100
Cost Approaches .................................................................................................................. 100
Income Approaches ............................................................................................................. 101
For Further Study .................................................................................................................. 110
Key Point Review .................................................................................................................. 110

7. Compiling Transaction Data for Decision Making .......................................................... 113

In This Chapter ..................................................................................................................... 114
Six-Step Preparation Process ............................................................................................... 115
Wrap Up ................................................................................................................................. 120

Resources ............................................................................................................................. 122
Web Sites ............................................................................................................................... 123
Currency Unions .................................................................................................................... 125
Glossary ................................................................................................................................. 126
Course Learning Goal

This course provides the tools and concepts real estate professionals need to serve clients and customers in the global real estate market. Students learn how to research markets, convert metric measures, monitor currency trends, alert clients to tax and visa matters, begin analyzing financial data for transactions, and follow a process for compiling transaction information.

Course Overview

- **Chapter 1: Researching a Market at Home or Abroad**
  A Country Assessment Model leads students through the process of compiling a dossier of market data—at home or abroad—interpreting the data, and identifying favorable characteristics.

- **Chapter 2: The Metric World**
  Because the USA does not use the metric system, U.S. real estate professionals must learn metric measures and conversion ratios in order to provide meaningful information on value, area, and distance to clients and customers from metric-system countries.

- **Chapter 3: Money Concepts**
  Availability of funds for a purchase and repatriation of income and sales proceeds are major factors for successful completion of transactions. By mastering currency concepts and monitoring key exchange rates, real estate professionals can help clients plan ahead to manage value fluctuation. Furthermore, learning to express values in a client’s home currency aids comprehension of the comparable and relative values of properties.

- **Chapter 4: Tax Matters**
  Foreign buyers and sellers want to know how U.S. tax law applies to them. Although real estate professionals should not give advice in tax matters, they should have a general knowledge of how real estate transactions involving foreign ownership are taxed.

- **Chapter 5: U.S. Visas**
  Foreign real estate owners want to know how U.S. visa regulations—entry to the country and permissible length of stay—may impact access to and enjoyment of their properties.

- **Chapter 6: Value Concepts**
  Commercial/investment clients and customers expect detailed financial analysis, but even buyers of vacation homes may expect to examine basic financial ratios. Real estate professionals must be
familiar with financial benchmarks and know how they are calculated and evaluated.

- **Chapter 7: Compiling Transaction Data for Decision Making**
  The six-step preparation process presented in this chapter leads real estate professionals through the process of compiling and synthesizing all of the information needed for a successful transaction.

**Learning Objectives**

- Research foreign and hometown markets and compile dossiers of market information.
- Evaluate markets’ pros and cons.
- Share information with clients and customers to help them make real estate decisions.
- Convert measurements between the metric system and U.S. system of measurements.
- Monitor currency value trends.
- Alert clients and customers to currency, fund transfer, and financing issues, and guide them to seek expert advice.
- Calculate currency conversions and express value in terms of a client’s home-country currency.
- Combine currency, area, and time calculations.
- Alert foreign clients and customers to tax considerations of real estate transactions.
- Begin to perform basic financial analysis using standard formulas.
- Compile, organize, and present financial data so that clients can make informed decisions.
- Follow a systematic approach to preparing for a transaction.
- Identify properties that meet the personal and investment objectives of clients and customers.
Exam

At the end of the course, participants will be given a 30-question open-book (unless closed-book is required for continuing education credit) multiple-choice exam to test and reinforce achievement of the course’s learning objectives. Successful completion is 80 percent, a total of 24 correct answers.

Activities and Class Procedures

This course incorporates a variety of activities designed to involve students, such as work group assignments, exercises, and discussions. Students are strongly encouraged to ask questions and engage in class discussions and group exercises. The range of experience levels among students offers a rich opportunity for learning from peers. Your active involvement will enrich the learning experience for yourself and others.

Earning the CIPS Designation

The NATIONAL ASSOCIATION OF REALTORS® awards the Certified International Property Specialist (CIPS) Designation to REALTORS® who complete the required coursework and demonstrate global real estate experience.

The CIPS course curriculum is the foundation for a worldwide network of real estate professionals in over 60 countries.

Course Requirements

To be eligible for the CIPS Designation, you must complete five of the courses listed below, including the prerequisite “Global Real Estate: Local Markets,” and complete an application demonstrating 100 points of international experience. From the time the first course is taken, you have three years to complete the coursework and apply for the designation.

- Global Real Estate: Local Markets (Both U.S. and non-U.S. students)
- Global Real Estate: Transaction Tools (U.S. students only)
- The Business of U.S. Real Estate (Non-U.S. Students only)
Three of the following elective courses:

- Europe and International Real Estate
- Asia/Pacific and International Real Estate
- The Americas and International Real Estate
- At Home with Diversity

One of the following courses can count as one elective option:

- CRS 200 – Business Planning and Marketing for the Residential Specialist
- CRS 204 – Creating Wealth through Residential Real Estate Investments
- CCIM – Residential Real Estate Financial Analysis
- One Real Estate Advanced Practices (REAP) module from the Council of Residential Specialists (CRS) (Non-U.S. students)

**International Real Estate Experience**

For up-to-date information on experiential requirements and a designation application form, go to www.Realtor.org/global.
1. Researching a Market at Home or Abroad
In This Chapter

- Researching markets
- Pro and con indicators
- Interpreting market data
- Applying the Country Assessment Model in your hometown market

How to use the information in this chapter

- Research data about both foreign and hometown markets
- Compile a dossier of market information
- Evaluate markets’ pros and cons
- Share information with clients and customers to help them make real estate decisions
Real estate buyers or sellers from other parts of the world rely on the real estate professional’s guidance and market knowledge to make decisions. When distance, language, and culture figure into the transaction, the real estate professional’s guidance gains even more importance.

In-depth market knowledge and the ability to apply it for a client’s advantage strengthen the real estate professional’s value proposition and competitive edge. A systematic approach to compiling and evaluating market data provides this knowledge base.

Because foreign buyers, such as commercial real estate investors and vacation-home buyers, compare areas as well as properties, you should have ready answers to questions about how your market compares to others. If your local market includes clients, such as expatriate retirees, who favor particular foreign locales or originate from a particular country, knowledge of that market area helps you fulfill the role of trusted real estate advisor and choose reliable referral partners.

The following research model provides a system for compiling and evaluating market information—at home or abroad.

**The Country Assessment Model**

The Country Assessment Model leads you through the process of compiling a dossier of market data. Information on interpreting the data and identifying favorable characteristics follows.

As you use this model to research, organize, and evaluate market information, keep in mind that:

- Data may not be readily available for each point of the checklist.

- You can decide how much detail to seek and how much time to spend pursuing it.

- Ongoing research keeps data up-to-date.
Country Assessment Model

**Geography**
- Major cities, states, provinces, colonies
- Climate, terrain, borders, and coastlines
- Unique features
- Environmental issues and agreements
- Natural resources

**Real Estate**
- Market size
- Private property rights
- Foreign ownership
- Acquisition costs, fees, and taxes
- Transaction support: MLS, records access
- Rental property: commercial, residential, office
- Land use regulation, zoning, permits
- Financing
- Brokerage practices and agent licensing
- Forms of ownership
- Role of the notary
- Investment returns and value appreciation
- Commercial trends
- Home ownership rates and housing trends

**Demographics**
- Population: size, age, density, trends
- Consumption and savings rates
- Per capita income
- Languages and literacy
- Labor force composition (service, industry, agriculture) and overall skill level

**Government**
- Type, structure, tenure, and stability
- Tax laws and rates (citizens, foreigners, corporate, capital, inheritance, tax treaties)
- Legal system and court structure
- Constitution, legislature, regulatory structure
- Major political parties and elections
- Voting rights
- Administrative structure and bureaucracy

**Economy and Business**
- Economic philosophy and monetary policy
- Base industries
- Currency and exchange trends
- Inflation, recession, and GDP trends
- Unemployment
- Major trading partners and alliances
- Exports and imports
- Trade balance
- Trade and capital flow restrictions
- Wage and price controls
- Business infrastructure
- Market access—internal and external

**Infrastructure**
- Electricity and water supplies, waste management
- Transportation and shipping: airports, ports, waterways, railways, roads
- Banking, ATMs, credit cards
- Technology usage
- Internet access
- Communications and media
- Institutions: medical, educational, religious

**Beyond the Basics**
- Ethnic composition
- Business impact of religion and culture
- Business and social behavior
- Traditions
- Holidays
- Negotiation and decision-making styles
- Mistakes to avoid

**Networking and Key Contracts**
- Potential clients and customers: corporate, commercial, individual, local, and foreign
- Business and professional connections
- Real estate organizations
- Real estate expositions and events
Interpreting Country Assessment Model Data

- **Geography**
  Knowledge of a country’s geography provides a context for understanding the structure of the market. Locations of major cities, capitals, ports, industrial areas, and resort areas usually coincide with the most active real estate markets and largest population centers.

  Divisions of a country into states, provinces, or administrative districts can indicate an organized approach to regulation and governance and development of civic institutions. The day-to-day governance of the country, however, must be examined to determine if administrative structures delegate regulatory authority to local governments or facilitate centralized control.

  Knowledge of climate, terrain, coastlines, and borders helps the researcher understand how the natural world shapes the way of life as well as the economy and business. For example, India’s monsoon season is a closely watched economic indicator; Mexico’s miles of coastline offer development opportunities for shipping facilities, such as the Punta Colonet port project and Fonatur resort destinations. In most cases, bordering countries are likely trading partners.

  Natural resources create and sustain a country’s wealth. A country poor in natural resources is import-dependent for resources such as the minerals necessary for modern industrial development. A country must, however, have the ability to access and use or export natural resources in order to create wealth; for example, the Central African Republic possesses rich mineral deposits but ranks as one of the world’s least-developed countries, with most of the population engaged in subsistence farming.

**Favorable Characteristics**

- Several population centers with a variety of industrial, commercial, housing, and resort developments
- Tourism
- Provincial or state administrative organization
- Borders with friendly trading partners
- Accessible natural resources
- Signatory to environment agreements
Real Estate
The real estate market’s size indicates both the volume and variety of transactions and the potential commission income. In the rental market, vacancy rates quantify the balance between supply and demand. Thus, increasing rents and decreasing vacancy rates indicate a landlord’s market. Lease terms also provide important comparison data.

Notary fees, commissions, stamp duties, land registration fees, transfer taxes, acquisition taxes, and value-added taxes all add to the cost of acquiring a property in a particular market. These costs vary widely between countries, states or provinces, and cities.

Favorable Characteristics

- Rational land use regulations
- Accessible and reliable property title records
- Market support: title, finance, property management, construction, insurance, engineering, architectural, appraisal, and brokerage
- Laws favoring private property rights and unrestricted ownership
- Balanced landlord-tenant laws and leasing terms
- Availability of affordable financing
- Good investment returns and value appreciation trends
- Market name recognition
- Availability of investment-grade properties
- Balanced leasing absorption and occupancy rates
- Competitive capitalization rates
- Real estate agents’ professionalism and licensing
1. Researching a Market at Home or Abroad

Demographics

Population growth drives demand for real estate, particularly for residential properties. Most economists, however, consider a growth rate of more than 2–3 percent too rapid for sustainable development. Population density influences the makeup of an economy and the types of real estate properties that serve it. Aging rates impact housing demand, too. A young population correlates to demand for housing, schools, retail, and jobs. Conversely, an aging population usually means less demand for all types of real estate, as well as economic pressures that pose challenges to growth. Some analysts see these pressures already at work in developed countries such as the U.S., Canada, Japan, and South Korea, where the median age of the population ranges from 37 to 46.

The size and composition of the labor force indicate the market’s attractiveness to foreign companies who hire local workers. The unemployment rate reveals an economy's actual compared to potential output. Distribution of the labor force among industry, agriculture, and services in comparison to productivity is another signal of economic balance. For example, the 53 percent of India’s labor force employed in agriculture produces only 17 percent of the country’s GDP; by contrast the service sector employs 28 percent of the labor force and produces 57 percent of the GDP.¹

Favorable Characteristics

- Sustainable population growth rate of 1–3 percent and a young population
- Reasonable consumption-to-savings ratio and increasing per capita income
- An educated, skilled workforce and high rates of literacy
- Job creation rate proportionate to population growth
- Low levels of unemployment and underemployment

Government

The powers, attitudes, structures, and stability of a government can determine the success or failure of the economy. Democracy, open markets, structural stability, tax incentives, and rational regulation are positive characteristics. Membership in trade agreements and

¹ CIA World Factbook, www.cia.gov
alliances denotes a cooperative approach to global trade and foreign investment.

A strong central government can be a benefit or a hindrance. Laws and regulations that emanate from a strong central government create countrywide standards, although implementation at provincial and local levels can be uneven. On the other hand, centralized regulation allows little adaptation to local conditions.

**Favorable Characteristics**

- Laws that preserve free markets and allow foreign-owned assets
- Few restrictions on ownership, capital flow, wages, and prices
- Anti-inflationary monetary policies
- Conservative fiscal policy and balanced budget
- Reasonable tax laws and rates on income, gains, sales, imports/exports, and corporations, for both domestic and foreign taxpayers
- Promotion of trade agreements and alliances
- History of stability
- Few government subsidies or tariffs

**Economy and Business**

A country’s economic philosophy shapes its business environment. Business, however, needs adequate infrastructure—communication systems, banking, corporate structures, and distribution systems—to support its functions. A survey of base industries, level of development, and the untapped potential indicate competitive standing in world markets. Ultimately, the resources, products, and industries of an economy describe its unique character and convey its level of advancement.

Inflation rates, including historical periods of recession or hyperinflation, measure the loss or gain of consumer purchasing power. Exchange rate trends show economic performance compared to other countries.

Developed economies have a mix of advanced manufacturing, agriculture, services, technology, and communications. Less developed economies, on the other hand, tend to have a large
portion of the workforce engaged in agriculture and labor-intensive industries.

Exports indicate the economy’s strengths and base industries. Imports point to the country’s shortcomings, needs, and wants. Trading partners can reveal the country’s economic alliances and dependencies. A positive trade balance between imports and exports means the production of exports outpaces the cost of imports.

**Favorable Characteristics**

- Globally traded currency
- Stable banking system and oversight of the money supply
- Stable or strengthening exchange rate values
- Steady growth of GDP
- Positive trade balance
- Existing foreign investment
- History of consistently low inflation rates
- Stable, competitive base industries, services, and distribution systems
- Availability of competent management
- Technological advancement
- Developed business infrastructure including communication systems and corporate structures

**Infrastructure**

A country cannot easily sustain economic growth in the absence of essential infrastructure. Many of the world’s emerging economies face difficult decisions about whether to invest in underdeveloped infrastructure to sustain and expand economic growth. Developed countries in Europe as well as the USA face issues with aging infrastructure. China, meanwhile, has invested heavily in a rapid expansion of its roads, airports, and bridges.

The CIA World Factbook (www.cia.gov) provides information on infrastructure issues for the world’s countries.
Favorable Characteristics

- Civic institutions, colleges, universities, hospitals, and medical facilities
- Reliable (and operating below capacity) water, power, and waste disposal systems
- Adequate supply of potable water
- Paved roads and highways
- Reliable transportation systems for people and goods

Beyond the Basics
A country’s ethnicities, languages, religions, traditions, and history create its unique identity. Understanding a nation’s culture facilitates working with its people and places business matters, including the ownership of real estate, in the context of broader cultural values and beliefs.

Favorable Characteristics

- Favorable cultural attitudes toward business, industry, and trade
- Informed views of world events, other nationalities, and cultures
- Religious and cultural norms that do not preclude open trade with other countries
- Women’s rights
- Cooperation, mutual respect, and harmonious relations between ethnic and religious groups

Networking
Consider your community in terms of its current global connections. Many cities, states, colleges, and other organizations sponsor international festivals and events, host overseas visitors, and set up exchanges or sister-city connections. Such programs indicate the interest in and extent of international activity in your area and offer a rich source for networking connections.
1. Researching a Market at Home or Abroad

**Favorable Characteristics**

- Business and real estate organizations
- Real estate events and expositions
- International organizations such as Rotary, Sister Cities
- International events

**Applying the Assessment Model in Your Home Market**

You can use the Country Assessment Model to compile detailed data on your hometown market area.

In the process of collecting and evaluating your local market’s potential for global business, you may discover untapped opportunities and new angles. Research the types of investments that have already occurred in your local market because these provide a good perspective of current opportunities. If other real estate professionals have identified a significant market demand, you can follow the trend or look for another approach.

**Discussion Question**

Based on the Country Assessment Model, are indicators positive or negative for your market area?
Skill Practice—Assessing Your Local Market

Use the Country Assessment Model categories to evaluate aspects of your local market’s potential for global business. List at least 1 favorable characteristic in each category. If the local market has many favorable attributes, it should be possible to find and transact international business. On the other hand, if the local market has negative attributes, think about how those drawbacks can be presented in a positive way.

<table>
<thead>
<tr>
<th>Favorable Characteristics</th>
<th>Negative Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Geography</td>
<td></td>
</tr>
<tr>
<td>Real Estate</td>
<td></td>
</tr>
<tr>
<td>Demographics</td>
<td></td>
</tr>
<tr>
<td>Government</td>
<td></td>
</tr>
<tr>
<td>Economy and Business</td>
<td></td>
</tr>
<tr>
<td>Infrastructure</td>
<td></td>
</tr>
<tr>
<td>Beyond the Basics</td>
<td></td>
</tr>
<tr>
<td>Networking</td>
<td></td>
</tr>
</tbody>
</table>
1. Researching a Market at Home or Abroad

www.Realtor.com/international allows you to search for properties in over 36 countries in 11 languages. Use the Country Assessment Model to conduct research on the markets in which those properties are located.
Key Point Review

- A systematic approach to researching, compiling, and synthesizing market data enables the real estate professional to evaluate and compare markets.

- In the process of collecting and evaluating your local market’s potential for global business, you may discover untapped opportunities and new angles.

- A knowledgeable real estate professional can help clients and customers compare markets as well as properties.

- Even if all foreign business is local market business, knowledge creates competitive edge. The ability to apply market knowledge to a client’s advantage creates an enduring value proposition.

- Aspects of a country—such as demographics, government, geography, climate, religion, and culture—shape economic life and real estate markets.
Next Chapter

In addition to market knowledge, real estate professionals must be able to communicate property values and area measurements in a way that clients and customers can understand. Just as people from foreign countries speak languages other than English, they use the metric “language” to measure quantities, distances, and areas, and their home country’s “currency language” to understand and evaluate value. The next chapters focus on using the metric system in real estate and understanding property values in foreign currencies.
In This Chapter

- The metric system applied in real estate
- Conversion formulas
- Estimating

How to use the information in this chapter

- Convert measurements between the metric system and the U.S. system of measurements
Every major global market except the USA uses the metric system of measurement. In order to participate in the global real estate market, U.S. real estate professionals need to know the “metric language” of measurement so that they can provide meaningful information on value, area, and distance to clients and customers from metric-system countries. Even immigrants who are long-time residents of the U.S. often continue to judge relative value in terms of metric measures. Converting square feet to square meters, and other metric measures, is like translating from one language to another using numbers instead of words to communicate value.

### Area

- **Convert square feet to square meters**
  - DIVIDE square feet by 10.7639
  - Square feet ÷ 10.7639 = square meters
  - **Example:** 12,916.68 square feet ÷ 10.7639 = 1,200 square meters

- **Convert square meters to square feet**
  - MULTIPLY square meters by 10.7639
  - Square meters x 10.7639 = square feet
  - 1,200 square meters x 10.7639 = 12,916.68 square feet

- **Convert price per square foot to price per square meter**
  - MULTIPLY price per square foot by 10.7639
  - Price per square foot x 10.7639 = price per square meter
  - **Example:** $50 per square foot x 10.7639 = $538.19 per square meter

- **Convert price per square meter to price per square foot**
  - DIVIDE price per square meter by 10.7639
  - Price per square meter ÷ 10.7639 = price per square foot
  - **Example:** $400 per square meter ÷ 10.7639 = $37.16 per square foot
Convert monthly cost to annual cost

Outside of the USA, rents are commonly quoted in cost per square meter per year.

- MULTIPLY cost per month by 12 to calculate the annual cost
- **Example:** $350 per square meter per month $x 12 = $4,200 per square meter per year

- DIVIDE the annual cost by 12 to figure the cost per month
- **Example:** $4,200 per square meter per year $÷ 12 = $350 per square meter per month

Estimating Area

When showing properties, there may be times when you must estimate area, whether in square feet or square meters. If you cannot calculate the conversion using the factor of 10.7639, a conversion factor of 10 can provide a reasonably close estimate; just be sure to qualify the estimate as “somewhat smaller” or “somewhat larger.” Exact figures can be provided later.

The following rule of thumb is easy to remember and provides a reasonable estimate.

- **DIVIDE** square feet by ten for an estimate of square meters.
  For example, 4,000 square feet is somewhat smaller than 400 square meters.

- **MULTIPLY** square meters by ten for an estimate of square feet.
  For example, 150 square meters is somewhat larger than 1,500 square feet.

Visit online app stores to add a metric conversion application to your phone.

For up-to-date information on useful apps for the real estate professional, visit REPurposed Apps, at www.repurposedapps.com. REPurposed Apps is an NAR member resource.
2. The Metric World

“Somewhat Smaller”

Square Feet ➔ Square Meters

“Somewhat Larger”

Square Meters ➔ Square Feet

Dimensions

Building features, such as kitchen cabinets, floor tiles, and windows, are measured in centimeters. One hundred centimeters equal one meter, which is slightly longer than one yard.

- **Convert centimeters to inches**
  - DIVIDE centimeters by inches
  - Centimeters ÷ 2.54 = inches
  - **Example**: 100 centimeters ÷ 2.54 = 39.37 inches

- **Convert inches to centimeters**
  - MULTIPLY inches by centimeters
  - Inches x 2.54 = centimeters
  - **Example**: 36 inches = 91.44 centimeters
Land

Large land areas, such as agricultural land, are measured in hectares. One hectare is 10,000 square meters, which is an area roughly the size of two soccer fields.

■ Convert hectares to acres

  - MULTIPLY hectares × 2.471 = acres
  - Example: 5 hectares × 2.471 = 12.355 acres

■ Convert acres to hectares

  - DIVIDE acres ÷ 2.471 = hectares
  - Example: 40 acres ÷ 2.471 = 16.1877 hectares

■ Convert acres to square meters

  - DIVIDE acres ÷ .0002471 = square meters
  - Example: 1 acre ÷ .0002471 = 4,047 square meters

■ Convert square meters to acres

  - MULTIPLY square meters × .0002471 = acres
  - Example: 3,000 square meters = .74 acres
Skill Practice

- Your client is looking for 4,000 square meters of warehouse space. Will a 35,000 square foot warehouse qualify? __________

- Convert 4,000 square meters to square feet. __________

- If a condominium unit is 1,700 square feet in size, what is the equivalent size in square meters? __________

- If a property rents for $35 per square foot per month, what is the monthly rent per square meter? __________

  What is the annual rent per square meter? __________

Notes:
**Let’s Go Metric!**

Land is measured in hectares, distance in kilometers, area in square meters, length in meters and centimeters, weight in grams and kilograms, and liquids in liters. Metric measurements are based on multiples of 10; for example, 100 centimeters equal 1 meter, 1,000 meters equal 1 kilometer, 1,000 grams equal 1 kilogram, 10,000 square meters equal 1 hectare.

<table>
<thead>
<tr>
<th>Measure</th>
<th>Convert from metric</th>
<th>Formula</th>
<th>Convert to metric</th>
<th>Formula</th>
<th>Which is larger?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Meter</td>
<td>1 meter = 3.28 feet, 1.03689 yards, or 39.37 inches</td>
<td>meters x 3.28 = feet</td>
<td>1 foot = .3048 meters</td>
<td>feet x .3048 = meters</td>
<td>A meter is larger than a foot or a yard</td>
</tr>
<tr>
<td>Square meter</td>
<td>1 sq meter = 10.7639 sq feet</td>
<td>sq meters x 10.7639 = sq feet</td>
<td>1 sq foot = .0929 sq meters</td>
<td>sq feet x .0929 = sq meters</td>
<td>A square meter is larger than a square foot or yard</td>
</tr>
<tr>
<td>Kilometer</td>
<td>1 kilometer = .621 miles</td>
<td>kilometers x .621 = miles</td>
<td>1 mile = 1.621 kilometers</td>
<td>miles x 1.621 = kilometers</td>
<td>A mile is longer than a kilometer</td>
</tr>
<tr>
<td>Hectare</td>
<td>1 hectare = 2.471 acres, 10,000 sq meters</td>
<td>hectares x 2.471 = acres</td>
<td>1 acre = .4047 hectares</td>
<td>acres x .4047 = hectares</td>
<td>A hectare is larger than an acre</td>
</tr>
<tr>
<td>Liter</td>
<td>1 liter = .264 gallons U.S.</td>
<td>liters x .264 = gallons U.S.</td>
<td>1 gallon U.S. = 3.79 liters</td>
<td>gallons U.S. x 3.79 = liters</td>
<td>A U.S. gallon is larger than a liter</td>
</tr>
<tr>
<td>Centimeter</td>
<td>1 centimeter = .3937 inches</td>
<td>centimeters x .3937 = inches</td>
<td>1 inch = 2.5 centimeters</td>
<td>inches x 2.5 = centimeters</td>
<td>An inch is longer than a centimeter</td>
</tr>
<tr>
<td>Kilogram</td>
<td>1 kilogram = 2.2 pounds</td>
<td>kilograms x 2.20 = pounds</td>
<td>1 pound = .453 kilograms</td>
<td>pounds x .453 = kilograms</td>
<td>A kilogram is heavier than a pound</td>
</tr>
<tr>
<td>Gram</td>
<td>1 gram = .0352 ounces</td>
<td>grams x .0352 = ounces</td>
<td>1 ounce = 28.349 grams</td>
<td>ounces x 28.349 = grams</td>
<td>An ounce is heavier than a gram</td>
</tr>
</tbody>
</table>
Key Point Review

- Conversions between metric and U.S. measures are simple multiplication or division calculations.

- The “magic number” for converting square meters or square feet is 10.7639.

- The conversion factor of 10.7639 can also be used to calculate price per square meter or square foot.

- Remembering which quantity or area is larger in size will help you remember whether to divide or multiply by the magic number.

- When it is not possible to do accurate calculations, dividing or multiplying by 10 will provide a close estimate; be sure to qualify the estimate by stating that the actual figure will be somewhat larger or smaller.

Notes:
Next Chapter

Now that we have learned how to calculate metric conversions, the next lesson adds the element of value. We will look at how to calculate relative values using currency conversion rates and how to combine calculations of currency value and square meters.
GLOBAL REAL ESTATE: TRANSACTION TOOLS

MONEY CONCEPTS
In This Chapter

- Major world currencies and currency unions
- Why currencies fluctuate
- Effect of currency fluctuations on real estate transactions
- Using exchange rates to convert values
- Combining currency and area calculations
- Moving money between countries
- Mortgage finance for foreign buyers

How to use the information in this chapter

- Monitor currency value trends

- Alert clients and customers to currency, fund transfer, and financing issues, and guide them to seek expert advice

- Explain the importance of having money in the country where the transaction takes place

- Calculate currency conversions and express value in terms of a client’s home-country currency

- Combine currency, area, and time calculations
Global real estate involves moving money between countries and converting currencies. Currency values fluctuate for a variety of reasons, such as investors’ view of a nation’s economic health, speculation, and government actions.

Currency value correlates closely with other indicators of economic strength. In simplest terms, stable exchange rates inspire investor confidence. A weak currency increases the cost of imports for consumers and cross-border investments for domestic investors, but creates opportunities for investors from strong-currency countries. For commercial and investment clients, exchange rate fluctuation adds another element of risk to transactions.

By monitoring exchange rates, real estate professionals can help clients plan ahead to manage value fluctuations and transfer transaction funds. Availability of funds for a purchase and repatriation of income and sales proceeds are major factors for successful completion of transactions. Furthermore, expressing values in a client’s home currency aids comprehension of properties’ comparable and relative values.

**Small Changes = Big Impact**

Real estate professionals need to be aware of the impact of currency values because even a small change can significantly increase or decrease:

- Price
- Sale proceeds
- Buying power
- Return on investment
- Gain or loss on sale
- Transaction costs
- Payment of loans, closing expenses, operating costs, and upkeep
- Rental income
- Commissions and referral fees
Currency Fluctuation: Offer to Closing and Beyond

Consider the following scenario. When a buyer signs a purchase contract the euro/US dollar exchange rate is US$1 = €0.80, but by the time of closing the exchange rate changes to US$1=€0.73. If a U.S. buyer offered €500,000 for a European property, made a 10% down payment, and closed 60 days later, the U.S. dollar amount needed to close the deal would be as follows:

<table>
<thead>
<tr>
<th>Purchase Price</th>
<th>Down Payment</th>
<th>Balance Due at Closing</th>
<th>Exchange Rate</th>
<th>US$ Amount to Close</th>
</tr>
</thead>
<tbody>
<tr>
<td>€500,000</td>
<td>- €50,000 =</td>
<td>€450,000 @</td>
<td>1US$=.80€</td>
<td>$562,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(1€ = $1.25)</td>
<td></td>
</tr>
</tbody>
</table>

As the dollar weakened, the amount needed to close increased.

<table>
<thead>
<tr>
<th>Purchase Price</th>
<th>Down Payment</th>
<th>Balance Due at Closing</th>
<th>Exchange Rate</th>
<th>US$ Amount to Close</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>€450,000@</td>
<td>1US$=.73€</td>
<td>$630,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(1€ = $1.40)</td>
<td>+ US$67,500</td>
</tr>
</tbody>
</table>

If the dollar strengthened to €0.83, the amount needed to close would decrease.

<table>
<thead>
<tr>
<th>Purchase Price</th>
<th>Down Payment</th>
<th>Balance Due at Closing</th>
<th>Exchange Rate</th>
<th>US$ Amount to Close</th>
</tr>
</thead>
<tbody>
<tr>
<td>€500,000</td>
<td>- €50,000 =</td>
<td>€450,000</td>
<td>1US$=.83€</td>
<td>$540,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(1€ = $1.20)</td>
<td>- US$22,500</td>
</tr>
</tbody>
</table>

If the situation were reversed, and a European buyer offered US$500,000 for a U.S. property, the euro amount needed to close would be as follows:

<table>
<thead>
<tr>
<th>Purchase Price</th>
<th>Down Payment</th>
<th>Balance Due at Closing</th>
<th>Exchange Rate</th>
<th>€ Amount to Close</th>
</tr>
</thead>
<tbody>
<tr>
<td>$500,000</td>
<td>-$50,000 =</td>
<td>$450,000 @</td>
<td>1€=US$1.25 ($1 = €.80)</td>
<td>€360,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

As the euro strengthened, the amount needed to close decreased.

<table>
<thead>
<tr>
<th>Purchase Price</th>
<th>Down Payment</th>
<th>Balance Due at Closing</th>
<th>Exchange Rate</th>
<th>€ Amount to Close</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>$450,000@</td>
<td>1€=US$1.40 ($1 = €.71)</td>
<td>€319,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- €40,500</td>
</tr>
</tbody>
</table>

If the euro weakened to US$1.20, the amount needed to close would increase.

<table>
<thead>
<tr>
<th>Purchase Price</th>
<th>Down Payment</th>
<th>Balance Due at Closing</th>
<th>Exchange Rate</th>
<th>€ Amount to Close</th>
</tr>
</thead>
<tbody>
<tr>
<td>$500,000</td>
<td></td>
<td>$450,000</td>
<td>1€=1.20US$ ($1 = €.83)</td>
<td>€373,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>+ €13,000</td>
</tr>
</tbody>
</table>
Exchange rate fluctuation affects value at all stages of the transaction. A foreign investor buys a property for a certain price at a certain time. When selling the property, the investor may discover that the real estate value has appreciated, but the relative value of domestic currency has decreased with the result that value appreciation and currency decline negate each other. On the other hand, when currency values fall buyers may try to store value in real estate, even if it has little possibility of value appreciation. If the value of the property appreciates, the investor reaps an additional reward at the time of sale.
Impact of Value of U.S. Dollar on International Sales

U.S. REALTORS® were asked how much the value of the dollar impacted international sales in their local markets. When a foreign country’s currency gains in value relative to the dollar, U.S. home prices are effectively less expensive to the foreigner than was the case prior to the change in currency values. The converse is also true.


Discussion Question

Refer to the diagram on the phases of a transaction. How does currency value fluctuation impact these phases of a real estate transaction?
Why Currency Values Fluctuate

The system of floating exchange rates is a legacy of the post-WWII Bretton Woods Conference, which established a fixed value for signatory countries’ currencies relative to the U.S. dollar and made them exchangeable for each other. The dollar, in turn, was tied to the price of gold and backed by a government-owned stockpile of bullion. In 1971, during a time of runaway inflation, the USA abandoned the gold standard. Consequently, world currencies now trade on the basis of perceived or projected value.

Currency value indicates a country’s economic strength because it correlates closely with the levels of business activity, gross domestic product, inflation, and employment. Stable exchange rates inspire investor confidence. The social, political, and economic environment all affect investor confidence and impact currency value.

- **Supply and demand**: Like any commodity, a currency increases in value when demand for it exceeds supply and loses value when supply exceeds demand. This does not mean that people no longer want the money; it means that they prefer to hold their wealth in some other form, like real estate or another currency. Supply-driven value increase results from growing demand for business transactions or speculation.

- **Speculation**: Currency and currency futures are traded on exchanges similar to the futures markets for commodities or options markets for equity stocks. Predetermined buy and sell orders activate when currencies reach preset values, adding volatility to the currency market. Central banks may try to manage speculative demand by buying or selling currency or adjusting interest rates. Favorable interest rates, for example, create demand for the currency.

- **Inflation**: Inflation erodes the worth of investments, causing currency value to drop and investment capital to flee. During times of high inflation, borrowing costs increase and savings rates decline as money in bank accounts loses value. Pre-inflation loans, which are repaid with inflated money, must be discounted or restructured to attract investors. During times of extreme inflation, or hyperinflation, a country’s currency becomes virtually worthless.
Governments try to influence exchange rates by setting a fixed rate, maintaining a rate range (known as a managed float), buying or selling currency, infusing capital markets with cash, printing more money, pegging to another currency, dollarizing, and revaluing.

- **Devaluation**: When a government allows or mandates devaluation, the currency loses value in relation to others. Devaluation usually results when a previously fixed-rate currency, perceived by investors as overvalued, is allowed to float. It provides a temporary solution for inflation or hyperinflation, but it cannot revive a faltering economy.

- **Dollarization**: When a country substitutes the currency of another country for its own, or another currency circulates and is accepted parallel to the official currency, it is termed dollarization. Dollarization, which can be any substitute currency, can be official government policy, such as in Panama, which uses U.S. currency but circulates its own coins, or de facto, when the population adopts parallel use of another currency. During times of high inflation, holding another country’s currency can be an informal hedge against lost savings and buying power.

- **Fixed-rate policy**: Governments maintain a fixed-rate policy by making it illegal to trade the currency on the open market, which often creates an active black market. However, currency value cannot adjust in response to external events that impact the domestic economy. Political and social upheaval may follow abandonment of a fixed-rate policy because the currency’s value resets to its true market value.

- **Pegging to another currency**: A currency may be fixed, or pegged, to another and move parallel with it. This action maintains a stable investment environment and encourages domestic savings. However, a pegged currency depends on the economic health, good or bad, of the other country regardless of domestic economic health. More commonly, governments peg currency rates within a trading range, a banded float, relative to another currency.

### Hard and Soft Currencies

A hard currency trades on currency markets and inspires investor confidence. Countries, especially government sovereign funds, store wealth by stockpiling hard currency funds. Hard currencies include the U.S. dollar, euro, Swiss franc, U.K. pound, Japanese Yen, Swedish krona, Canadian dollar, Norwegian krone, Australian dollar, New Zealand dollar, and gold. Note that all of the hard-currency countries have capitalistic
systems, private property rights, and thriving real estate markets. As eloquently stated by Hernando DeSoto in *The Mystery of Capital* “The connection between modern money and capital is through real property.”

A soft currency generally experiences greater fluctuation; consequently, investors and other countries do not want to hold it. This is not a reflection on the economy (South Korea, China, and Brazil are all soft-currency countries with dynamic economies) but the market’s perception of the currency as a store of wealth and value. Some soft currencies are pegged to another country’s currency, such as the East Caribbean dollar, which is pegged to the U.S. dollar, or trade at a fixed rate. The artificial values of pegged and fixed-rate currencies seldom reflect the country’s economy vitality.

**Currency Unions**

When a group of countries agree to use a common currency it is known as a currency or monetary union. The European Union’s euro is the world’s largest, most influential, and perhaps most controversial currency union. The majority, though not all, of the nations in the European Union have adopted the euro as their currency. Although the United Kingdom, Denmark, and Sweden are EU members, they have not converted to the euro. While the events in the EU have demonstrated the risks of different economies, of varying strengths and weaknesses, joining fates and sharing responsibility, currency unions can facilitate cross-border trade by eliminating the cost and exchange rate risk of currency conversion. These unions also tend to synchronize the business cycles of participating countries. Other currency unions are the Central and West African Franc and the Eastern Caribbean Dollar. (See page 125 for a list of participating countries.)

**Advantage or Disadvantage?**

The basic principle of currency fluctuation is relative value. When currency A strengthens against currency B, more units of currency B are needed to purchase an equivalent amount of currency A. This movement benefits holders of currency A, but harms holders of currency B.

A strengthening home-country currency creates an advantage for global buyers and generally is a favorable economic trend; however, it can increase the prices of a country’s exports and make them less competitive in the global market. When a country cannot find buyers for its exports, cheaper imported products flood the market and skew the balance of trade. A rapid influx of foreign investment in a particular economic sector, such as oil or natural gas, can boost the value of the
country’s currency, and make the cost of exports from other economic sectors, such as manufacturing or agriculture, less affordable for trading partners.

Think of currency value as temperature and the exchange rates as layers of clothing added or removed as the temperature rises or falls.

<table>
<thead>
<tr>
<th>Disadvantage</th>
<th>Advantage</th>
</tr>
</thead>
<tbody>
<tr>
<td>When the temperature drops (value decreases), you need more layers of clothing (more units of currency) to maintain body temperature (value).</td>
<td>When the temperature rises (value increases), you need fewer layers of clothing (fewer units of currency) to maintain body temperature (value).</td>
</tr>
</tbody>
</table>

Managing Exchange Rate Risk

What can the real estate professional do to help clients manage the impact of exchange rate fluctuation? When working with buyers, during the initial counseling session, real estate professionals should:

- Ask where and in what currency the transaction funds are held.
- Stress the importance of transferring and converting the funds as soon as possible, and describe the consequences of delay. If the buyer must wait for money to be transferred and converted before making an offer, the opportunity to purchase a first-choice property could be lost. A seller may not accept an offer conditioned on transferring the money from another country.
- Explain the need to determine an appropriate price range and move quickly when the right property is found.
3. Money Concepts

- Caution that if the funds are not available to close a transaction on the contracted date, the buyer risks losing the down payment.

Sophisticated, risk-tolerant investors may try to manage exchange rate risk by buying or selling currency futures as a hedge. Currency futures are traded on major exchanges for the Australian dollar, British pound, Canadian dollar, euro, Japanese yen, Mexican peso, New Zealand dollar, Swiss franc, and U.S. dollar. This aggressive strategy is best used by knowledgeable investors because it magnifies both gains and losses if the currency market moves to the investor’s advantage or disadvantage. On a large transaction even a small fluctuation has a huge cost-impact, which is further magnified, positively or negatively, by leverage.

**Exchange Rate Web Sites**

The financial sections of major newspapers and Web sites publish up-to-date exchange rates:

- **HiFx Currency Converter**—www.hifx.com
- **Universal Currency Converter**—www.xe.com
- **www.OANDA.com**
- **eXchangeRate.com**—www.exchangerate.com
- **CoinMill.com**—http://coinmill.com
- **MSN Money Currency Converter**—http://investing.money.msn.com/investments/currency-converter-calculator
- **Exchange rates and exchange rate history**—www.exchange-rates.org

Several of these sites provide the code to embed their tools directly in your Web site.
Using Exchange Rates to Convert Values

- **Convert from your home currency to a foreign currency**
  - MULTIPLY home currency by the exchange rate

  **Example 1: U.S. dollars to euros**
  $200 \times .75 = €150$

  **Example 2: Japanese Yen to Indian Rupees**
  Y500 \times .51 = Rs255

  **Example 3: Canadian dollars to Chinese Yuan**
  $1,500 \times 6.43 = ¥9,645$

- **Convert foreign currency to your home currency**
  - DIVIDE the foreign currency by the exchange rate

  **Example 1: Euros to U.S. dollars**
  €150 \div .75 = $200

  **Example 2: India Rupees to Japanese Yen**
  Rs255 \div .51 = Y500

  **Example 3: Chinese Yuan to Canadian dollars**
  ¥9,645 \div 6.43 = $1,500
Skill Practice—Currency Conversion

Calculate the following currency conversions using the sample exchange rates shown in parentheses:

<table>
<thead>
<tr>
<th>Home Currency</th>
<th>Equivalent Amount</th>
<th>Exchange Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Euro</td>
<td>€5,762</td>
<td>(1.73)</td>
</tr>
<tr>
<td>2. U.S. Dollars</td>
<td>US$25,000</td>
<td>(46.62)</td>
</tr>
<tr>
<td>3. Japanese Yen</td>
<td>¥6,345</td>
<td>(.007)</td>
</tr>
<tr>
<td>4. British Pounds</td>
<td>£33,649</td>
<td>(1.63)</td>
</tr>
<tr>
<td>5. U.S. Dollars</td>
<td>US$75,725</td>
<td>(.61)</td>
</tr>
<tr>
<td>6. Chinese Yuan</td>
<td>¥1,650</td>
<td>(.10)</td>
</tr>
</tbody>
</table>

Now, imagine that upon return from a trip your wallet contains the following amounts of currencies. If all of these currencies are converted to U.S. dollars, what is the total amount of U.S. dollars you will have? Use the sample exchange rates shown.

- 400 Euros
  \[ 400 \div 0.75 = \]
- 87 Japanese Yen
  \[ 90 \div \frac{89.91}{1} = \]
- 620 Chinese Yuan
  \[ 620 \div 6.83 = \]
- 50 Swiss Francs
  \[ 50 \div 1.03 = \]

Total U.S. Dollars?
Combining Foreign Currency and Area Measures

When properties are listed in terms of local currency and measurements, there are three elements in a real estate transaction that need conversion: **currency, area, and time**.

Some practitioners use the word CAT to remember the sequence of calculations for converting currency, area, and time.

1. Convert **Currency**

2. Convert **Area** and price per area unit

3. Convert **Time**—monthly to annual or annual to monthly

- **Example**: An apartment in Kobe, Japan rents for ¥4,000 per square meter per month. Your U.S. client would like to know the equivalent price in dollars per square foot per year. (Assume US$1 = ¥88.51)

  1. **Currency**
     
     ¥4,000 ÷ 88.51 = US$45.19 per square meter/month

  2. **Area**

     US$45.19 ÷ 10.7639 = US$4.20 per square foot/month

  3. **Time**

- **Example**: A 150-square-meter retail space in Mexico City rents for 90,000 pesos per square meter per month. What is the cost per square foot per year in U.S. dollars? (Assume $US1 = MP 14.286).

  1. **Currency**

     90,000 pesos ÷ 14.286 = $6,300 per square meter per year

  2. **Area**

     $6300 ÷ 10.7639 = $585.29 per square foot per year

  3. **Time**

     $585.29 ÷ 12 = $48.77 per square foot per month
Example: Your U.K. client wants to buy a condo in Miami. The unit must be at least 100 square meters and maximum annual rent cannot exceed £10,000. What square footage and monthly rent should you look for? (Assume US$1 = £.61)

1. Currency
   £10,000 ÷ .61 = $16,393.44

2. Area
   100 square meters x 10.7639 = 1,076.39 square feet

3. Time
   $16,393.44 ÷ 12 = $1,366.12
### Global Real Estate: Transaction Tools

#### 1. Convert home currency to foreign currency

\[
\text{Home currency} \times \text{exchange rate} = \text{foreign currency}
\]

- **US dollars to Japanese yen:** \(\text{US}\$1,500 \times 89.91 = ¥134,865\)
- **Euros to Chinese yuan:** \(€1,500 \times 8.91 = ¥14,865\)

#### 1. Convert foreign currency to home currency

\[
\text{Foreign currency} \div \text{exchange rate} = \text{home currency}
\]

- **Japanese yen to US dollars:** \(¥134,865 \div 89.91 = \text{US}\$1,500\)
- **Chinese yuan to euros:** \(¥14,865 \div 9.1 = €1,500\)

#### Put it all together

The rental rate on an apartment in Kobe, Japan, is quoted at ¥4,000 per square meter per month. Your U.S. client would like to know the equivalent price in dollars per square foot per year.

1. **Currency**

\[¥4,000 \div 89.91 = \text{US}\$44.48 \text{ per M}^2/\text{month}\]

2. **Area**

\[\text{US}\$44.48 \times 10.7639 = \text{US}\$4.13 \text{ per square foot per month}\]

3. **Time**

\[\text{US}\$4.13 \times 12 = \text{US}\$49.56 \text{ per square foot per year}\]

An alternate method for calculating an equivalent currency value is multiplying by the reciprocal. Divide 1 by the exchange rate to calculate the reciprocal.

#### Reciprocal exchange rate

\[
1 \div \text{foreign currency exchange rate} = \text{reciprocal}
\]

\[¥1 \div 89.91 = \$0.01112, \text{US}\$1,500 \times 0.01112 = ¥134,865\]
Methods for Moving Money Between Countries

Wire Transfer
Wire transfer moves large amounts of money between banks quickly and securely. The funds are withdrawn directly from a bank account and transferred electronically to another bank account. The transfer process usually takes 24 to 72 hours to complete and most banks charge a fee for the transfer.

In order to move funds by wire transfer, the initiator needs to know the recipient bank’s International Bank Account Number (IBAN), Bank Identifier Code (BIC), or Society for Worldwide Interbank Financial Telecommunication (SWIFT) code. The bank’s staff can provide these numbers. The IBAN is used almost universally these days although some institutions still use the SWIFT code or BIC number, both of which are holdovers from the days of the Telex.

Check
Money transferred by check—cashier’s check or personal check—moves very slowly. A personal check may not be accepted. If the check is accepted for deposit, the bank will likely delay crediting the funds to the depositor’s account until the check has fully cleared. The process of clearing the check can take several weeks to months. If an exchange of currency is involved, the bank may assess a fee or commission.

Cash
The riskiest method for transferring funds is cash. Most countries, including the USA, require travelers to declare large amounts of cash on arrival. Many countries also place limits on the amount of cash that a traveler may legally carry out of or into a country. It should be obvious that these regulations are aimed at preventing criminal activities and money laundering.

Furthermore, the 1970 Bank Secrecy Act requires U.S. banks to report to the IRS any cash transaction of more than $10,000.

ATM
With today’s worldwide banking networks, travelers can access funds through global ATM networks. Immigrant workers sometimes use the ATM system to make money available to their families back home. Family members can use ATM cards to withdraw funds deposited by the worker. However, most banks or ATMs place a limit on how much money a user
can withdraw in a 24-hour period, making ATMs largely impractical for securing funds for large transactions.

**Repatriation**

Repatriation of funds means transfer of income or sale proceeds from a foreign transaction to the recipient’s home country. The USA, Canada, and European Union countries place few restrictions on a foreign property owner’s repatriation of funds. Other countries are more restrictive.

Repatriation of funds involves three issues:

- **Establishing source:** there should be a clear paper trail for the funds from the time of first arrival in the country, through all phases of investment, sale, and repatriation.

- **Exchange rate:** as noted earlier, exchange rate fluctuation may increase or erode value.

- **Taxes:** when large sums are involved, such as property sale proceeds, applicable taxes must be paid. Hence, the purpose for FIRPTA withholding, which we will look at in the next chapter.

**Mortgage Finance for Foreign Buyers**

NAR research shows a significant percentage of foreign buyers purchase U.S. properties with cash. In 2013, 63 percent of foreign buyers paid cash. What is driving this trend is not that foreign buyers are more awash in cash than before, although family members or close friends may pool resources to purchase property. The simple fact is that foreign buyers have a difficult time obtaining mortgage financing. When foreign buyers’ credit histories, ratings, and financial profiles don’t correspond to U.S. lenders’ underwriting procedures, the buyers, despite their creditworthiness, have difficulties obtaining mortgage loans.
3. Money Concepts

Islamic Financing
Because the Koran forbids paying or receiving interest on loans, banks have developed Islamic (Murabaha) financing to facilitate purchases of homes and businesses. In simplest terms, the lender purchases the asset on behalf of the borrower and “sells” it to the borrower on a deferred, cost-plus basis. Banks that offer Islamic financing set policies on when the borrower must take possession of the asset and begin payments.

Key Point Review
- Currency fluctuation impacts all phases of a real estate transaction, increasing or decreasing gains and losses as relative values change.
- Currency value fluctuates when demand for it exceeds supply, or vice versa. Inflation and speculative trading also impact currency value.
- Government actions can impact currency value, such as fixed- or pegged-rate policies or devaluation. Dollarization occurs when a country substitutes another’s currency for its own—as a de facto or formal policy.

Hard currencies are traded internationally and inspire investor confidence. Soft currencies are less desirable as a store of wealth even though some of the world’s most dynamic economies are soft-currency countries.

A strengthening home-country currency is, in most cases, an advantage.

A foreign buyer should have funds in the country in which the transaction will take place so that opportunities are not lost.

The three elements of a real transaction that need conversion are Currency, Area, and Time (CAT).

A fast and secure method for moving large sums of money between countries is the wire transfer.
Next Chapter

As we have learned in this chapter, currency value fluctuation is a major factor in real estate transactions. Even small changes in exchange rate can amplify losses or gains on a transaction. Currency value, however, is only one financial aspect of the transaction. Foreign buyers and sellers want to know how U.S. tax law will impact them.
In This Chapter

- Taxpayer status—resident and nonresident
- Physical and substantial presence tests
- Income taxes for foreign property owners
- Capital gains tax
- Estate tax
- Foreign Investment Real Property Tax Act (FIRPTA)
- Nontax reporting requirements

How to use the information in this chapter

- Alert foreign clients and customers to tax considerations of real estate transactions
- Guide clients and customers to seek expert advice on tax matters
Foreign buyers and sellers want to know how U.S. tax law applies to them. Although real estate professionals should not give advice in tax matters, they should have a general knowledge of how real estate transactions involving foreign ownership are taxed. When real estate professionals know about tax regulations and processes, they can alert their clients to tax considerations and guide them to seek expert advice.

As a basic principle, all transactions by foreign buyers and sellers of U.S. real estate are U.S.-sourced and therefore subject to U.S. taxes on income and sales. Foreign individuals who meet certain criteria are also subject to U.S. income tax. Failure to comply in a timely manner with U.S. tax regulations can trigger serious consequences for a buyer, seller, or real estate professional.

**Taxpayer Status**

The primary consideration in determining how federal tax laws apply to foreign investors is residency. U.S. citizens and residents are taxed on worldwide income. A foreign person—neither a U.S. citizen nor a legal resident—is taxed on U.S.-sourced income. All transactions in U.S. real property are considered sourced in the USA.

<table>
<thead>
<tr>
<th>Definition of Resident Status for U.S. Tax Purposes</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Citizen .......................... Taxed on worldwide income; credits are allowed for foreign taxes paid</td>
</tr>
<tr>
<td>Resident Alien .................... Taxed on worldwide income; credits are allowed for foreign taxes paid</td>
</tr>
<tr>
<td>Nonresident Alien ........ Taxed only on U.S.-sourced income</td>
</tr>
</tbody>
</table>

**Caution**: Do not confuse these tax-resident definitions with immigration and visa classifications.
Tax Treaties

The United States maintains tax treaties with a number of countries. These agreements do not necessarily limit or reduce the amount of taxes due in relation to the U.S. real property interest, but they do prevent double-taxation.

If a tax treaty overrides or modifies IRS requirements, the taxpayer may reduce or avoid withholding by completing IRS form 8833—Treaty-Based Return Position Disclosure.

Tax treaties change frequently. For up-to-date information on U.S. tax treaties go to www.irs.gov and type “treaties” in the search bar.

Substantial Presence

Nonresident aliens are considered U.S. residents for income tax purposes (not immigration) if they meet the substantial presence test²:

- Physically present in the United States for at least 31 days in the current year, and
- 183 days during the three-year period that includes the current and two preceding years, counting:
  - Total number of days present in the USA during the current calendar year, plus
  - One-third of the days present during the immediately preceding calendar year, plus
  - One-sixth of the days present during the second preceding year

Example: A nonresident alien is present in the USA for 150 days in the current year, 65 days in the immediately preceding calendar year, and 32 days in the second preceding calendar year. The application of the substantial presence test is:

<table>
<thead>
<tr>
<th>Days</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>150</td>
<td>Current year</td>
</tr>
<tr>
<td>+ 65</td>
<td>More than one-third of 150</td>
</tr>
<tr>
<td>+ 32</td>
<td>More than one-sixth of 150</td>
</tr>
<tr>
<td></td>
<td>247 days</td>
</tr>
</tbody>
</table>

In this case, the nonresident alien is considered a U.S. resident for tax purposes (not immigration).

Even if a foreigner meets the substantial presence test, he may qualify as a nonresident for tax treatment by filing IRS Form 8840—Close Connection Exception Statement for Aliens. In order to claim this exception the taxpayer must maintain a tax home in a foreign country. The exception cannot be claimed if the individual has applied for U.S. residency.

Taxpayer Identification Number

In order to transact real estate business in the USA, a Taxpayer Identification Number (TIN) is required. A foreign corporation may obtain an Employer Identification Number (EIN).

For U.S. citizens and residents, the Social Security Number (SSN) serves as a taxpayer identifier. Those who are not eligible to receive an SSN can apply for a TIN by completing IRS Form W-7 Application for IRS Individual Taxpayer Identification Number. Processing time for a TIN takes several weeks—allow 8–10 weeks. Because a real estate deal cannot close without this identification number, foreign buyers and sellers should apply for a TIN well in advance of a planned transaction. Information and application forms are available at www.irs.gov.

When making an application for a TIN, the information on the form must be confirmed by a valid foreign passport. If a valid passport is not submitted, the applicant must submit at least two (or more) current photo ID documents as verification. For most applicants, the documents must be original or certified copies; notarized or Apostilled copies are not accepted.
Income Tax for Foreign Real Estate Owners

Income earned from real estate by nonresidents generally falls under one of two tax arrangements: 30 percent withholding or effectively connected income.

- **30 Percent Withholding**
  Income from real estate, such as rental income, is a passive activity that is subject to a flat-rate withholding tax of 30 percent on gross income (not net). No deductions are allowed for operating expenses, interest payments, or repairs.

- **Effectively Connected Income (ECI)**
  If a foreign person carries on a trade or business in the USA, income from that enterprise is deemed “effectively connected income” and tax is imposed on net income according to the same graduated rates paid by U.S. residents. Deductions are allowed for operating and other expenses in relation to the business.

**Net Basis Election**

The IRS views ownership of real estate as a passive activity (unless other participation tests are met), which is not considered engagement in a U.S. trade or business.

A foreign real estate owner may, however, **elect** to be taxed on a net basis as though the income is connected with a U.S. trade or business. Once this election is made, it cannot be changed without IRS approval. This means that a foreign taxpayer cannot switch between taxation on a net basis one year and 30 percent withholding gross basis the next unless authorized by the IRS.

Failure to file tax returns on a timely basis can risk loss of the ECI election and make rental income subject to the 30 percent withholding requirement.

Electing to be taxed on a net basis avoids costly withholding on gross income and allows deductions for operating expenses, which reduces tax liability. The choice between the net tax election or 30 percent withholding on gross must be considered in the context of the taxpayer’s overall tax liability—both in the USA and worldwide. A real estate professional can make clients and customers aware of these choices and guide them to seek expert advice.
Property Manager as Withholding Agent

The IRS views a real estate professional who collects rents on behalf of a foreign owner as a withholding agent. As such, the real estate professional can be held personally liable for any taxes that must be withheld and paid. The withholding agent must withhold 30 percent of a foreign owners’ rental income unless a certification of exemption is completed with the IRS (Form W-8ECI) including a Taxpayer Identification Number (TIN).

FACTA

New regulations under the Foreign Account Tax Compliance Act (FACTA), effective in 2014, target tax non-compliance by U.S. taxpayers with foreign accounts, but have broader implications for transactions with foreign investors. FATCA requires foreign financial institutions (FFIs) and U.S. withholding agents to implement new procedures for tax information reporting and withholding, account identification, and documentation. It also requires certain FFIs to enter into an agreement with the U.S. (an FFI Agreement). As an alternative, certain countries have entered into intergovernmental agreements (IGAs) with the U.S. to overcome legal impediments that prevented FFIs from entering into FFI Agreements with the U.S.³

Because these regulations are in the process of being implemented, real estate professionals should consult tax professionals to determine the implications for themselves, their companies, and their clients.

Taxable Income from Real Estate

In order to figure taxable income, cost recovery allowance, interest expense, and amortized points are subtracted from net operating income (NOI); NOI is calculated by subtracting expenses from gross operating income.

\[ \text{NOI} - \text{Cost Recovery} - \text{Interest} - \text{Amortized Points} = \text{Taxable Income} \]

Remember that all income from U.S. real estate is considered U.S. sourced, which means the owner must pay U.S. income tax regardless of the taxpayer’s citizenship, residency status, or tax home. The income received by the individual owner is taxed as ordinary income.

³ IRS, PwC
Mortgage Point Amortization

A pro-rata annual portion of mortgage points and loan origination fees is deductible, amortized over the life of the loan. If the loan term is 15 years, \( \frac{1}{15^{th}} \) (6.6 percent) of the cost of points and fees may be deducted annually.

Cost Recovery

Cost recovery, or depreciation, allows the property owner to recover a portion of the cost of an asset as an annual tax deduction. It is based on the idea that things—buildings, equipment, vehicles—wear out over time and lose economic value. Land, however, is never depreciable. Non-residential real estate is depreciated on a straight-line basis over a period of 39 years. This means that \( \frac{0.02564}{1 ÷ 39} \) of the cost is allowed each year as a tax deduction. Residential rental property is depreciated over a period of 27.5 years, which means \( \frac{0.03636}{1 ÷ 39} \) of the cost is deducted each year. Cost recovery deductions lower the owner’s basis in the property, thus increasing the amount of capital gain on the sale. If the sale of a property results in a gain, the amount of the gain attributable to depreciation is recaptured and taxed at a rate of 25 percent. Depreciation recapture is figured into the gain on sale even if the taxpayer did not claim cost recovery deductions.

Foreign Investment in Real Property Tax Act (FIRPTA)

A foreign owner’s first contact with the U.S. income tax system may occur at the time of sale, when money is withheld to comply with the Foreign Investment in Real Property Tax Act (FIRPTA).

The basic requirement of FIRPTA is this: when a U.S. real property is purchased from a foreign seller, the buyer, or withholding agent, must withhold 10 percent of the sale price—not net proceeds—and forward the amount to the IRS within 20 days after the transaction closing.

The actual amount of tax will be calculated and paid when the seller files an income tax return. Any excess taxes paid from the 10 percent withholding will be returned to the seller.

The process of FIRPTA withholding and reporting may be handled as part of the transaction closing. The withholding agent may be an attorney, a CPA, or the real estate broker. A withholding agent who fails to properly withhold and report may be liable for the tax. This can have very serious consequences, particularly if there are large sums of money involved, as is often the case in real estate transactions.
Transactions may be exempt from FIRPTA withholding if:

- The buyer acquires the property as a personal residence and the purchase price does not exceed $300,000.

- The IRS provides a statement to the buyer that the seller is exempt from withholding or has made satisfactory arrangements.

- The seller furnishes an affidavit certifying that the seller is not a foreign person.

Real estate professionals for the buyer or seller can be held liable for up to the amount of their commissions if they fail to disclose to the buyer their knowledge of the sellers’ false certifications or false claims of exemption from withholding.

FIRPTA does not require disclosure of a foreign person’s identity during the ownership phase of a U.S. real property investment, but it does necessitate disclosure of identity on various documents at the time of sale.

**FIRPTA and Commercial Real Estate**

Under FIRPTA, a foreign investor who holds U.S. real estate as a passive investment (i.e., with any type of net lease) must withhold 30 percent of the gross rental income. This includes expenses that net-lease tenants pay.

The 10 percent withholding provisions described above apply to the sale of commercial properties. This regulation is particularly costly to a foreign seller if the sale will be at a loss or if the foreign seller’s tax liability will be less than the 10 percent withholding. The foreign seller can apply to the IRS for a reduction of the withholding; however, the IRS review can take up to 90 days. During this time the seller does not have access to the funds that exceed the amount he or she will ultimately owe in taxes.4

Because these withholding requirements inhibit foreign investment in commercial real estate, the U.S. Senate has proposed changes to FIRPTA. These changes would provide additional exemptions, particularly for real estate investment trusts (REITs). The changes have yet to become law, but you should monitor the progress of the legislation, called the Real Estate Investment and Jobs Act of 2013.

---

FIRPTA Flowchart

Start Here

Is property involved a U.S. real property interest? (USRPI)

no

yes

Is transferor a foreign person? (corporation, individual, partnership, estate, trust)

no

yes

Did withholding agent receive an exempt withholding certificate for the transaction?

no

yes

Withholding must be done and submitted on Form 8288 by the 20th day after the transaction.

If foreign corporation, did corporation receive an 897(i) election acceptance letter?

no

yes

No withholding is required.

Is USRPI in a domestic corporation where stocks are regularly traded on an established securities market?

no

yes

Did transferee purchase the property for $300,000 or less to be used as a personal residence?

no

yes

Is transferee making installment payments on USRPI that was disposed of prior to 1/1/85?

no

yes

Is transferee the U.S. government, a state, possession, or political subdivision of the U.S. or the District of Columbia?

no

yes

5 U.S Internal Revenue Service
Capital Gains Tax

Gains and losses on the sale of a U.S. real property interest are taxed as though the seller was engaged in a U.S. trade or business. The gain or loss on the sale is taxed the same as if the seller were a U.S. resident.

The amount the owner will receive at the time of sale is calculated by subtracting the mortgage balance and cost of the sale from the sales price. The result is the net sale proceeds before taxes, but it is not the amount on which capital gains tax is due. In order to figure capital gains tax liability, adjusted basis must be calculated.

Adjusted Basis

In order to determine the after-tax sale proceeds, the amount of capital gains tax due must be calculated. This calculation begins by determining the seller’s adjusted basis in the property. The formula is as follows:

\[
\text{Adjusted Basis} = \text{Purchase Price} + \text{Capital Improvements} - \text{Accumulated Cost Recovery}
\]

To calculate the amount of taxable gain, the adjusted basis and selling costs are subtracted from the sales price.

\[
\text{Capital Gain} = \text{Sales Price} - \text{Selling Costs} - \text{Adjusted Basis}
\]

The current (2013) maximum capital gain tax rate is 20 percent.

1031 Tax-Deferred Exchanges

Foreign individuals (nonresident aliens) and companies who own income or investment property in the USA may take advantage of 1031 tax-deferred exchanges. The transaction does not require U.S. citizenship or residency for either party, but both the exchanged and relinquished properties must be located in the U.S. The tax code for 1031 exchanges defines the USA as the fifty states, the District of Columbia, and the U.S. Virgin Islands.

Capital gains on the sale of real estate are always taxable. If a client wants to dispose of greatly appreciated property, subject to hefty capital
gains tax, and reinvest in U.S. property, a 1031 tax-deferred exchange offers advantages.

Tax-deferred exchanges are very complex transactions and require the involvement of experts, particularly a qualified intermediary. The REALTORS® Land Institute offers a course on 1031 Exchanges. For more information, visit www.rliland.com.

**Four Basic Rules of 1031 Exchanges**

1. Property must be held for investment or productive use in trade or business; dealer property does not qualify.
2. Property must be exchanged for like-kind property.
3. Replacement properties must be identified within 45 days after the relinquished property is transferred.
4. The exchange must be completed (replacement property received) by the earlier of 180 days or the tax return due date.

**Estate Tax**

The estates of foreign owners of U.S. real estate are subject to federal estate tax on assets in the USA. The substantial presence test does not apply for estate tax purposes. Instead, a series of facts and circumstances such as length of U.S. residence, statements of intent, and style of living in the USA and abroad determine whether the person is domiciled in the U.S. The application of these facts and circumstances is subjective in nature, and it is important for real estate professionals to direct clients and customers to a professional tax consultant experienced in estate tax issues to advise on estate tax liability. Federal estate and gift tax exemptions and credits available to U.S. citizens are available to foreign real property owners depending on their resident or nonresident status.

A non-citizen surviving spouse is potentially in a very expensive estate tax situation. The IRS looks at intent to remain in the USA and views a non-citizen surviving spouse as likely to leave the country. Consequently, the estate is not eligible for the marital deduction, which essentially allows a residence and other assets to pass to the surviving spouse free of estate tax. The entire value of jointly owned property is included in the estate assets, which makes the total value of the estate subject to estate tax at a top rate of 40 percent. Non-citizen surviving spouses can mitigate tax liability through a Qualified Domestic Trust (QDT).

Foreigner property owners should monitor U.S. estate tax developments and seek the guidance of a tax expert. In addition to federal taxes, some
states impose estate tax on assets or inheritance tax on bequests received by heirs.

**Forms of Ownership**

How a nonresident foreigner owns U.S. real property impacts its taxation during the period of ownership and upon sale. Some owners, particularly owners of large or complex investment properties, may prefer to form corporate entities to own real estate assets as a way to manage taxes, lessen or avoid estate taxes, and maintain privacy. The most advantageous form of ownership must be selected based on the owner’s overall tax profile and objectives. Setting up the corporate ownerships described on the next page requires expertise in corporate law and finance.

Although the owners may form a corporate entity for the primary purpose of managing federal taxes, it is important to remember that corporate entities are governed by the laws of the state in which the company is incorporated and subject to state corporate taxes too.

**Direct Ownership**

The simplest form of ownership is direct ownership—by an individual or partnership. It affords the owner direct control over the property. As covered in the preceding material, the owners are subject to income tax on revenue generated by the property and the owner must file an individual tax return. Because the buyer must supply a taxpayer identification number, ownership of the property is publicly identified. FIRPTA withholding requirements must be met when the property is sold, and federal estate tax must be considered. On the other hand, income from the property is taxed only once, as individual income to the owner, instead of the double taxation associated with corporate ownership.
Indirect Ownership through a U.S. Entity

Foreign owners may set up a U.S. corporate entity to own real estate assets as a way to manage income and capital gains taxes, maintain privacy, and limit liability. Clients and customers should seek legal and tax expertise to choose the form of ownership that best suits their interests.

Following are the different types of ownership entities:

- **Sole proprietorship**: This entity is inseparable from the individual owner, who is responsible for all business income and losses through payment of individual taxes.

- **General Partnership**: A general partnership is similar to a sole proprietorship in that each of the individual owners is liable for income taxes on his or her share of the business income. Partners are also personally liable for the actions and debts of the partnership.

- **Limited Partnership**: This entity is structured around a “general partner” and “limited partners,” who have invested in the enterprise. The general partner runs the business and is responsible for all business actions and debts, while limited partners have little control over day-to-day operations but are not liable for debts. This type of ownership is generally unpopular, except for large, complicated real estate development investments.

- **Limited Liability Corporation (LLC)**: LLCs limit personal liability for debts and lawsuits associated with a business, but income is passed directly to the owners of the corporation, who pay taxes on their share of the business income through their personal tax filing.

- **C Corporation**: The C corporation, named for the relevant tax code, is treated as an independent legal entity and a separate entity for tax purposes. It is separate from those who own, control, and manage it. The C corporation pays corporate tax, and the owners pay personal income tax only on their salaries, bonuses, and dividends. The C corporation has the disadvantage of double taxation—once at the corporate and again at the individual stockholder’s level.

- **S Corporation**: This entity, named for the relevant tax code, limits the liability of the owners, but income passes through to the owners, who pay personal income tax on corporate profits, even while the corporation reports those taxes under its own corporate tax returns. Owners pay taxes on their salaries, bonuses, and dividends as well as retained earnings they might need to leave in the corporation for planning purposes.
**Indirect Ownership through a Foreign Entity**

For sophisticated investors and complex investments, the most advantageous move may be formation of a foreign corporation whose sole asset is the stock of a U.S. corporation, which in turn acquires the real property. Ownership through a foreign corporation may offer some tax relief if a tax treaty exists with the owner’s tax home country. Foreign-entity ownership offers more privacy than direct or U.S. corporate ownership and may help the owner avoid U.S. estate taxes. The owner holds stock in the corporation, which in turn owns the real property asset. A nonresident foreigner who sells stock in a company does not pay U.S. capital gains tax on the profit. When the corporation owns real estate, however, the seller must be able to prove less than 5 percent ownership over the preceding 5-year period in order to avoid FIRPTA withholding. Furthermore, indirect ownership through a foreign entity may make the corporation subject to a branch profits tax.

**State and Local Regulations**

As noted above, a corporation or partnership is subject to the regulations and tax codes in the state in which the entity is organized. In addition, some state laws restrict or regulate foreign land investment and require ownership disclosure. Many states also have withholding laws similar to federal FIRPTA. A foreign property owner may not be familiar with these laws; it is important for a real estate professional to make foreign clients and customers aware of the laws and regulations that may impact them and refer them to experts such as corporate and tax specialists.

**Federal Reporting Requirements**

Foreign owners of some U.S. real estate are subject to federal reporting requirements unrelated to the tax code. These reports primarily gather information and protect consumers. These reporting requirements are mostly a concern for owners of large commercial, investment, and development projects, but purchases of small parcels of agricultural land must also be reported. The real estate professional should be able to alert clients and customers to these reporting requirements and guide them to seek expert advice in complying with the regulations; failure to comply with the regulations can result in stiff penalties.

- **International Investment and Trade in Services Act**
  Bureau of Economic Analysis (www.bea.gov/fdi)
  - **What to report:** any U.S. business enterprise in which a foreign person or company owns directly or indirectly a 10 percent or more voting interest.
Global Real Estate: Transaction Tools

- **When to report:** an initial report is required within 30 days of the end of the quarter in which the transaction took place. An annual report is required if business assets, sales or gross operating revenues, or total income are all $40 million or less (positive or negative). Quarterly reports are required if business assets, sales or gross operating revenues, and total income were each $60 million or less (positive or negative) for the most recent financial reporting year. A benchmark survey is conducted every five years.

- **Exemptions:** no annual report is required if foreign voting ownership falls below 10 percent. No quarterly report is required if it is owned indirectly by a foreign company or has no direct transactions with the foreign owner. No report is required for real estate used as a personal residence.

### Interstate Land Sales Full Disclosure Act

Consumer Financial Protection Bureau (www.consumerfinance.gov)

- **What to report:** any foreign or domestic development that involves subdivision of 100 or more lots must register with CFPB and provide a property report to purchasers before any contract is signed. The developer may be any individual or business that directly or indirectly sells, leases, offers, or advertises to sell or lease lots in a subdivision through a common promotional plan. Note that this definition does not apply to the one who does the actual physical development.

- **When to register:** regulations and processes for registration and reporting are being revised after administration of the law was passed from HUD to the CFPB. Visit the CFPB Web site for more information.

### Agricultural Foreign Investment Disclosure Act (AFIDA)

USDA Farm Service Agency (www.fsa.usda.gov)

- **What to report:** purchase of agricultural land by a nonresident alien, foreign company, or government. The transaction must be reported if it involves 10 acres or more of land that was used for farming, ranching, or timber production within the preceding 5 years, or if under 10 acres and produces annual revenues of $1,000 or more.
4. Tax Matters

- **Who must report:** a nonresident foreign person (including a nonpermanent resident for immigration purposes) or foreign entity that holds a substantial and significant interest. This is defined as 10 percent or more ownership by an individual, or 50 percent or more ownership if the individual owners do not act in concert and no one individual owns an interest of 10 percent or more.

- **When to report:** the initial transaction must be reported within 90 days to the county-level Farm Services Agency (FSA) office. A follow-up report is required if the land changes hands or use of it changes from agricultural to nonagricultural or vice versa.

**State Reporting Requirements**

In addition to the federal reporting and registration requirements, about 30 states require qualifying developers, and their agents involved in marketing the properties, to register with state governments. In some cases, the state regulations are more stringent than federal requirements. The purpose of state regulations is to provide jurisdiction over developers who market properties in the state and prevent consumer fraud. State laws may provide a right of rescission in cases of violations.

State laws vary but generally regulate developments of subdivided land with at least 10 or more units.

Laws apply only to a real estate salesperson directly representing a developer for multiple units in the development, not single-unit transactions such as a broker listing of a single unit in a development.

State laws vary, but generally require an initial registration and an annual renewal.

**Federal Tax Publications and Forms at www.irs.gov**

- Income Tax: Form 1040NR US Nonresident Alien Income Tax Return
- Taxpayer Identification Number: Form W-7 Application for IRS Individual Taxpayer Identification Number
- Foreign Tax Home Exception: Form 8840 Closer Connection Exception Statement for Aliens
Global Real Estate: Transaction Tools

- Modification of Withholding Due to Tax Treaty: Form 8833 Treaty-Based Return Position Disclosure

- FIRPTA
  - Form 8288: U.S. Withholding Tax Return for Dispositions by Foreign Persons of U.S. Real Property Interests
  - Form 8288A: Statement of Withholding on Dispositions by Foreign Persons of U.S. Real Property Interests
  - Form 8288B: Application for Withholding Certificate for Dispositions by Foreign Persons of U.S. Real Property Interests

- Publications
  - Publication 514: Foreign Tax Credit for Individuals
  - Publication: 515: Withholding of Tax on Nonresident Aliens and Foreign Entities
  - Publication 519: U.S. Tax Guide for Aliens
  - Publication 523: Selling Your Home
  - Publication 527: Residential Rental Property
  - Publication 530: Tax Information for Homeowners
  - Publication 544: Sales and Other Dispositions of Assets
  - Publication 550: Investment Income and Expenses
  - Publication 551: Basis of Assets
  - Publication 901: U.S. Tax Treaties
  - Publication 946: How to Depreciate Property
  - Publication 950: Introduction to Estate and Gift Taxes
Key Point Review

- Residency is the primary consideration in determining how federal tax laws apply to foreign property owners. U.S. citizens and residents are taxed on worldwide income. A foreign person—neither a U.S. citizen nor a legal resident—is taxed on U.S.-sourced income.

- All transactions in U.S. real property are considered sourced in the USA.

- Nonresidents’ trade or business income generally falls under one of two different tax arrangements: flat-rate withholding tax of 30 percent on gross income, or “effectively connected income” taxed on net income. A foreign real estate owner may elect to be taxed on a net basis as though the income is connected with a U.S. trade or business.

- The IRS views a real estate professional who collects rents on behalf of a foreign owner as a withholding agent who can be held personally liable for any taxes that must be withheld and paid.

- Foreigners must obtain a Taxpayer Identification Number (TIN) in order to transact real estate business in the United States.

- FIRPTA requires the buyer (or a withholding agent) of a U.S. real property from a foreign seller to withhold 10 percent of the sale price—not net proceeds—and forward the amount to the IRS within 20 days after the transaction closing. The property is exempt if the buyer acquires it as a personal residence and the purchase price does not exceed $300,000. FIRPTA requires a 30 percent withholding on passive investments, including gross rental income from commercial real estate net leases.

- Gains and losses on the sale of a U.S. real property interest are taxed as though the seller was engaged in a U.S. trade or business. The gain or loss on the sale is taxed the same as if the seller were a U.S. resident. Foreign investors are eligible to benefit from 1031 tax-deferred exchanges.

- Federal estate and gift tax exemptions and credits available to U.S. citizens are available to foreign real property owners depending on their resident or nonresident status. Non-citizen surviving spouses are generally not eligible for estate and gift tax exemptions.
Global Real Estate: Transaction Tools

- How a nonresident foreigner owns U.S. real property impacts its taxation during the period of ownership and upon sale. Corporations and partnerships are subject to the regulations and tax codes in the state in which the entity is organized.

- Foreign owners of some U.S. real estate are subject to federal reporting requirements. About 30 states require qualifying developers, and their agents involved in marketing the properties, to register with state governments.

Notes:
Next Chapter

Foreign clients often want to know what U.S. visa requirements impact them and their ability to visit and stay in the country. General knowledge of visa requirements will help the real estate professional direct clients to expert advice on visa matters.
GLOBAL REAL ESTATE: TRANSACTION TOOLS

5 U.S. VISAS
In This Chapter

- Types of U.S. visa statuses
- Work permits

How to use the information in this chapter

- Identify how foreigners are permitted to enter the U.S., how long they may stay, and for what purposes
- Recognize available visa statuses for foreign real estate owners and investors
- Guide foreign clients and customers to seek expert advice
Foreign real estate owners want to know how U.S. visa regulations—entry to the country and permissible length of stay—may impact access to and enjoyment of their properties.

The U.S. government places few restrictions on ownership of real estate by foreign individuals and companies. However, for foreign owners (non-citizens and nonresidents) access to their U.S. properties may be limited in terms of permissible entry and length of stay. With the exception of countries enrolled in the Visa Waiver Program, Canada, and Mexico, the U.S. has rather stringent requirements for entering and remaining in the country and seeking employment.

Although real estate professionals should not offer advice about immigrations and visa matters, they should be aware of visa regulations. General knowledge of visa matters helps the real estate professional alert foreign buyers and sellers so that they can seek expert advice and make informed decisions. Additionally, information on visas can provide valuable data on foreign investors in local markets. The U.S. Department of Homeland Security tracks nonimmigrant admissions into the country, and the findings are summarized in NAR’s State-by-State International Business Reports.

**Visa Waiver Program**

The Visa Waiver Program (VWP) allows citizens of the following countries to travel to the United States for business or pleasure without a visa and stay for 90 days. Those who wish to stay longer should apply for a visa.

<table>
<thead>
<tr>
<th>Andorra</th>
<th>France</th>
<th>Liechtenstein</th>
<th>Singapore</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>Germany</td>
<td>Lithuania</td>
<td>Slovakia</td>
</tr>
<tr>
<td>Austria</td>
<td>Greece</td>
<td>Luxembourg</td>
<td>Slovenia</td>
</tr>
<tr>
<td>Belgium</td>
<td>Hungary</td>
<td>Malta</td>
<td>South Korea</td>
</tr>
<tr>
<td>Brunei</td>
<td>Iceland</td>
<td>Monaco</td>
<td>Spain</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>Ireland</td>
<td>Netherlands</td>
<td>Sweden</td>
</tr>
<tr>
<td>Denmark</td>
<td>Italy</td>
<td>New Zealand</td>
<td>Switzerland</td>
</tr>
<tr>
<td>Estonia</td>
<td>Japan</td>
<td>Norway</td>
<td>Taiwan</td>
</tr>
<tr>
<td>Finland</td>
<td>Latvia</td>
<td>Portugal</td>
<td>United Kingdom</td>
</tr>
</tbody>
</table>
VWP visitors may view and purchase residential or business property, survey sites for an investment or business venture, and sign contracts. They may not, however, remain in the country to manage a business or seek employment.

**Type of Passport**
VWP travelers must possess machine-readable passports with digital photos. Depending on when the passport was issued and what country issued it, some travelers must also have a passport with an integrated chip that contains passport data (e-Passport). A traveler whose passport is valid but not machine-readable or, if applicable, an e-Passport, must obtain a visa.

**Electronic System Travel Authorization (ESTA)**
Visa Waiver Program travelers must complete an ESTA application online prior to travel. The ESTA process, a security measure adopted in 2009, determines eligibility for entry. Once approved, the ESTA is good for two years and allows multiple entries.

**Canadian Citizens**
Canadian citizens do not fall under the VWP. They may stay in the USA for up to six months. Entry by land requires proof of citizenship and a valid picture ID. If arriving by air, a passport is required.

**Visas for Personal and Business Travel**
Travelers must complete visa procedures before traveling to the United States.

**B-1 Business Visa**
The B-1 Business Visa permits:

- Consultation with business associates
- Negotiation of contracts
- Purchase of goods or materials
- Attendance at a conference or convention
- Performance of research
- Appearance as a witness in a court proceeding
- Participation in short-term training
5. U.S. Visas

- Settlement of an estate
- Survey of business and investment sites

The B-1 Visa holder may receive reimbursement of expenses, but not U.S.-sourced salary, wages, or consulting fees. Direct management of a business is not allowed. Permitted stay is the length of time deemed fair and reasonable in which to accomplish the intended activity, up to a maximum of 6 months; a B-1 Visa holder may obtain one extension, up to a maximum stay of one year. Spouses and dependents traveling with the B-1 Visa holder must apply separately for a B-2 visa.

**B-2 Pleasure/Tourism Visa**

A B-2 Pleasure/Tourism Visa permits:

- Touring and sightseeing
- Visiting relatives and friends
- Undergoing medical treatment
- Attendance at a conference or convention of a social or fraternal organization

A B-2 Visa holder may not engage in any business activity or receive any salary, wages, consulting fees, or expense reimbursement.

**L-1 Intracompany Transferee**

- Applies to individuals who own or work for foreign corporations directly related to U.S. corporations. Executive, managerial, or special-knowledge employment is required. Maximum stay, with an initial stay of three years and two-year extensions, is seven years. Visa holders may be accompanied by a spouse and unmarried children under 21 years of age.

  - This visa also enables a foreign company that does not yet have an affiliated U.S. office to send an executive, manager, or employee with specialized knowledge to the U.S. to establish or help establish such an office.
E-1 Treaty Trader
- Granted to individuals from countries that have a treaty of trade and commerce with the USA. The visa is initially granted for a two-year stay; extensions may be granted in two-year increments, with no maximum number of extensions. Visa holders may be accompanied by a spouse and unmarried children under 21 years of age.

E-2 Treaty Investor
- Permits a foreign individual to reside in the USA while actively investing in, operating, and managing a U.S. business.

EB-5 Immigrant Investor
The EB-5 Immigrant Investor visa is available to immigrants seeking to enter the U.S. to invest in a business in a Regional Center\(^6\), an economic unit, public or private, that promotes economic growth in a defined geographical area.

The following requirements apply to the EB-5 visa:
- The investment must be at least US $1 million.
  - If the business is in a designated target employment area—by law, a rural area or an area that has experienced high unemployment of at least 150 percent of the national average—the minimum initial investment is US $500,000.
- The commercial enterprise, which can be either a new business or an investment in a troubled business, must benefit the U.S. economy by providing goods and services to U.S. markets.
- The business must create full-time employment for at least 10 U.S. workers. This includes:
  - U.S. citizens
  - Lawful U.S. residents or others lawfully permitted to work in the U.S.

It does not include the investor, spouse, or sons and daughters.
- If the investment is to benefit a troubled business, pre-investment employment levels must be maintained for at least two years.

---

\(^6\) To see a current list of Regional Centers by state, visit the USCIS Web site, www.uscis.gov.
The investor/visa holder must be involved in the day-to-day management of the business or be involved in managing business policy (e.g., as a corporate officer or board member).

Visa holders may be accompanied by a spouse and unmarried children under the age of 21.

**Applying for the EB-5 Immigrant Investor Visa**

Application for the EB-5 Immigrant Investor visa is a three-step process:

1. Obtain approval of Form I-526 Petition for an Alien Entrepreneur. Certain documentation such as a comprehensive business plan and evidence that funds are lawfully sourced must accompany the form.

2. Either file an I-485 application to adjust status to lawful permanent resident, or apply for an immigrant visa at a U.S. Consulate or Embassy outside the U.S. The EB-5 applicant is granted conditional permanent residence for a two-year period upon the approval of the I-485 application or upon entry into the United States with an EB-5 visa.

3. File Form I-829 Petition by an Entrepreneur to Remove Conditions 90 days prior to the two-year anniversary of the granting of the EB-5 applicant’s Green Card.

**H-1B Specialized Occupations**

- Enables an individual with a bachelor’s degree, from the USA or abroad, to remain in the country for 6 years while employed in a professional position with a U.S. employer.

**H-2B Temporary Non-Agricultural Workers**

- Allows U.S. employers or U.S. agents who meet specific regulatory requirements to bring foreign nationals to the USA to fill temporary nonagricultural jobs. This visa is particularly relevant to resort areas, for employers filling seasonal employment needs.

**O1 and P1 Extraordinary**

- Provided for individuals of extraordinary ability in the sciences, arts, education, business, or athletics.
Arrival in the U.S.

Automated I-94 Form

Previously a paper form, the I-94 Form, which documents arrival and departure of visitors to the U.S., has been automated by the U.S. Customs and Border Protection (CPB) at air and sea ports of entry. The electronic I-94 record is available at the CPB Web site for travelers who need the information for verification of alien registration, immigration status, or employment authorization. Usually, travelers will not receive a paper form when traveling. Instead, CPB provides travelers with an admission stamp on their passport that is annotated with date of admission, class of admission, and “admitted until” date. Departure is recorded automatically using commercial carrier manifest data.

Most visa categories allow an extension of stay if the application is made before expiration of the current authorized stay. Eligibility for an extension is verified by CPB through the electronic I-94 record. Visa Waiver Program visitors may not apply for an extension.

US-VISIT Program

All foreign visitors are screened at admission and enrolled in the Department of Homeland Security US-VISIT program. This involves a digital fingerprint scan and photo, which may be collected again upon departure.

The US VISIT program does not apply to most Canadian citizens or Mexican citizens who do not travel outside of the border area or stay for more than 30 days.
Visitor Being Screened According to US-VISIT Requirements

Source: Wikipedia; public domain

Working in the United States

Of the visa statuses mentioned above, only the H-1B Specialized Worker, H-2B Temporary Non-Agricultural Worker, and L-1 Intracompany Transferee allow the individual to accept employment. The B-1 Business Visa allows the individual to conduct business and receive reimbursement of expenses but does not allow direct management or payment of a salary or consulting fee. In order to accept employment, the individual must obtain the appropriate permit. An authorization to seek employment should not be confused with residency status.

Trade NAFTA (TN) Worker Visa

As a result of the NAFTA agreement, citizens of Canada and Mexico may apply for a TN Workers Visa in 60 professional categories, most of which require a college (BA) degree and professional experience. The worker must meet the qualifications and also receive a job offer from a U.S. employer. The TN Visa is valid for up to 3 years and may be extended for additional terms.
Employment Authorization Document (EAD)

Certain classifications of visa holders such as refugees, students, and spouses of diplomats, treaty traders and investors, and intracompany transferees may apply for an EAD. If the application is approved, the individual receives an EAD card, which proves to prospective employers the individual’s permission to seek employment. A job offer from an employer is not required.

www.state.gov

It is not the goal of this course to cover the complexity of U.S. immigration regulations and procedures, which change frequently. This brief overview provides only basic information. Advise clients and customers to contact the U.S. Consulate in their home countries to learn about visa requirements and fees. Locations of U.S. Consulates and Embassies are listed on the U.S. State Department Web site at www.state.gov.

5 Tips for Choosing an Attorney to Assist with Visa Issues

1. **Do your homework:** Talk with your colleagues about their experiences with finding attorneys as part of their trusted network. Research the backgrounds and experience of attorneys you are considering adding to your network.

2. **Find out the attorney’s specialty:** Attorneys may handle one particular type of client, from a specific region, background, or purpose for coming to the U.S. Or they may specialize in one specific visa type.

3. **Check references:** The attorney should be able to provide three references, either from other real estate professionals or from clients.

4. **Ask about pricing:** Some attorneys will handle visa issues for a fixed price, rather than an hourly fee, which can accumulate.

5. **Ask about premium processing:** Some attorneys will expedite processing of visa cases for an additional fee. While you should advise clients to handle visa matters well in advance of deadlines, you will inevitably encounter a client who needs or desires a quicker response time from an attorney.

---

7 Adapted from “Coming to America: 5 Tips for Choosing a Visa and a Lawyer,” Forbes, www.forbes.com
Key Point Review

- The Visa Waiver Program (VWP) allows citizens of specific countries to travel to the United States for business or pleasure without a visa and stay for 90 days; those who wish to stay longer should apply for a visa. Visa Waiver Program travelers must complete an ESTA application online prior to travel.

- VWP visitors may view and purchase residential or business property, survey sites for an investment or business venture, and sign contracts; they may not remain in the country to manage a business or seek employment.

- Canadian citizens do not fall under the VWP. They may stay in the U.S. for up to six months. Entry by land requires proof of citizenship and a valid picture ID. If arriving by air, a passport is required.

- The B-1 Business Visa permits consultation with business associates, negotiation of contracts, purchase of goods or materials, and reimbursement of expenses. It does not allow U.S.-sourced salary, wages, or consulting fees or direct management of a business.

- The B-2 Pleasure/Tourism Visa allows touring, sightseeing, visiting relatives and friends, and staying at resorts. It does not allow any business activity salary, consulting fees, or expense reimbursement.

- The EB-5 Immigrant Investor visa is available to immigrants seeking to enter the U.S. to invest in a business in a Regional Center, an economic unit, public or private, that promotes economic growth in a defined geographical area.

- Other types of visas include:
  - Treaty Trader
  - Intracompany Transferee
  - Treaty Investor
  - Temporary Professional Worker
  - Temporary Non-Agricultural Worker

- In order to accept employment, an individual must obtain an Employment Authorization Document, which should not be confused with residency status.
Canadian and Mexican citizens who receive a job offer from a U.S. employer may apply for a TN Workers Visa; the TN Visa applies to 60 professional categories, most of which require a college (BA) degree and professional experience.

**Notes:**
The Next Chapter

In the preceding chapters we have learned how currency values, tax regulations, and visa status can impact the foreign real estate owner. We also learned how to convert currency values and area measurements. In the next chapter we will look at some of the value indicators investors examine when comparing and selecting properties.
In This Chapter

- How investment and business buyers compare values
- Sales, cost, and income approaches for determining value
- Helping buyers make informed decisions

How to use the information in this chapter

- Begin to use approaches to valuing investment properties
- Identify properties that meet the personal and investment objectives of clients and customers
In the previous chapters we have looked at considerations that impact real estate decisions for foreign buyers and sellers. We have examined how to research markets, convert currency and areas, help clients and customers manage currency fluctuation, and assess potential tax liability. We will now examine the approaches used to evaluate and compare investments.

Commercial/investment clients and customers expect detailed financial analyses, but even vacation-home buyers, who often view their second home as an investment, may expect to examine basic financial ratios. Therefore, real estate professionals should be familiar with commonly used approaches for valuing investment property. Financial analysis of large commercial/investment real estate deals, however, can be quite complicated. Unless the real estate professional is knowledgeable and skilled in the field, complex number crunching is probably best left to accountants and specialists in the field. Therefore, the real estate professional should identify experts who can provide specialized knowledge, skills, and judgment.

For real estate professionals skilled in financial analysis, a great resource for data is the Realtors Property Resource® (RPR), a wholly owned subsidiary of NAR. RPR provides users with comprehensive data, powerful analytics, and dynamic reports to meet the demands of clients. RPR is free to REALTORS® and has tools for agents, brokers, commercial professionals, appraisers, associations, and MLSs.

In this chapter, we will examine commonly used financial ratios. The intent is to expose you to the ratios, not for you to gain a thorough understanding. Later in the chapter, there is information about where to go for further, in-depth study on valuing investment property.
RPR, free to REALTORS, provides data and other resources useful for financial analysis. Visit www.narpr.com.
Four Investment Elements

Before we examine methods for determining value, let's look at two important concepts: the elements of an investment and the time/value of money.

- Elements of the an investment
  - Yield
  - Safety
  - Leverage
  - Control

- Time/value of money

Yield

Yield, or rate of return, is the dollar amount earned on each dollar invested over the life of the investment. Two types of return or yield are:

- Return of capital—return of the initial amount invested
- Return on capital—profit generated from the investment

Desired yield or return depends on an investor’s objective. For example, an investor who wants to protect capital may pay a higher price (resulting in a lower yield) than one seeking to maximize cash flow and income. On the other hand, if value appreciation, instead of income, is the main objective, an investor may be willing to accept a lower rate of return. Risk-averse investors may pay more for safe properties and knowingly accept lower returns.
Safety

The three basic sources of investment risk are:

- Loss of capital
- Loss of return on capital
- Opportunity cost—the capital lost because the investor was unable to invest it

Global investors may also incur country risk, which involves factors such as currency losses, nationalization of property, and unfavorable regulatory changes.

Leverage

Leverage, sometimes referred to as OPM (other people’s money), involves using borrowed money to make investments with the hope that return on the investment will exceed the cost of borrowing. Examples of leverage include buying equity stock on margin or financing a real estate purchase with a mortgage.

Positive leverage results when the yield exceeds the cost of the borrowed funds. Conversely, negative leverage occurs when the cost of borrowed funds exceeds the investment yield. Rapid value appreciation or advantageous currency trends can offset negative leverage.

Example:

A client has the opportunity to invest in an office building. The client can purchase the office building all cash, or put 25 percent down and get a loan for the remaining 75 percent.

Calculating the returns on both alternatives, given the client’s investment objectives, reveals the following:

- An all-cash investment will yield a return of 5 percent.
- Financing the investment, with the associated borrowing costs, will yield a return of 4 percent.

In this example, the return on the leveraged transaction is lower than the return on the unleveraged transaction. This is an example of negative leverage. While the office building may be producing a positive cash flow and appreciating in value, the leveraged money is not producing better results than purchasing with all cash, everything else being equal.
Control

The first three investment elements—safety, yield, and leverage—are linked directly to market conditions. Control, on the other hand, depends on personal preference and access to the property. Control issues vary among properties and the investor’s expectations of personal involvement. Passive investors (not to be confused with the IRS definition) invest their money and allow others to operate the investment. Actively involved investors want to manage most aspects of the investment.

Time/Value of Money

The time/value of money is an important concept for understanding valuation of properties, particularly income-producing ones. Simply stated, the principle of the time/value of money is this: the value of a sum of money received today is greater than the value of the same amount in the future. Would you rather receive $1,000 today or $1,000 in the future? Isn’t the sum the same?

The answer depends on two factors—inflation and opportunity cost. Opportunity cost is the return that can be gained if the money is invested, or lost if the money is idle. Inflation decreases buying power. Money in hand today is more valuable than the same amount received in the future because of lost opportunity for investment growth and decreased buyer power. Of course, risk is also a factor but there is no risk if you have the money in hand now instead of anticipating future receipt of money from an investment.

Example:

Idle money loses value. Therefore, the value of a sum of money received in the future is less than the same amount today. What is the present value of $1,000 in three years if the annual inflation is 2 percent?

<table>
<thead>
<tr>
<th>Year</th>
<th>Present Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Year 1</td>
<td>$980.00</td>
</tr>
<tr>
<td>Year 2</td>
<td>$960.40</td>
</tr>
<tr>
<td>Year 3</td>
<td>$941.19</td>
</tr>
</tbody>
</table>
Example:
What if the money is invested? If an investment earns an annual return of 3.5 percent, what is the future value of $1,000 after three years?

<table>
<thead>
<tr>
<th>Year</th>
<th>Future Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>$1,035</td>
</tr>
<tr>
<td>2</td>
<td>$1,071.23</td>
</tr>
<tr>
<td>3</td>
<td>$1,108.72</td>
</tr>
</tbody>
</table>

$1,000 Present Value

Time/value calculations involve the functions of compounding and discounting, which underlie investment performance calculations such as net present value.

- **Compounding**
  Compounding occurs when invested money gains value. Think of money deposited in a savings account. The deposit grows because each interest calculation incorporates the initial deposit plus accumulated interest.

- **Discounting**
  Discounting converts future values to present value. Think of it as the interest that must be paid on a loan’s present value—the amount that must be paid in the future to settle a debt.

- **Opportunity Cost**
  Investments can be compared on the basis of opportunity cost, which is the rate of return that could be achieved by an alternative investment. Or it can be viewed as the loss incurred due to selection of the current investment.
7/10 Rule

How long does it take for an investment to double in value? The 7/10 rule is a handy estimator of future value. A sum invested at 10 percent will double in 7 years, or if invested at 7 percent, it will double in 10 years.

<table>
<thead>
<tr>
<th>n</th>
<th>i = 7%</th>
<th>i = 10%</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>107.00</td>
<td>110.00</td>
</tr>
<tr>
<td>2</td>
<td>114.49</td>
<td>121.00</td>
</tr>
<tr>
<td>3</td>
<td>122.50</td>
<td>133.10</td>
</tr>
<tr>
<td>4</td>
<td>131.08</td>
<td>146.41</td>
</tr>
<tr>
<td>5</td>
<td>140.26</td>
<td>161.05</td>
</tr>
<tr>
<td>6</td>
<td>150.07</td>
<td>177.16</td>
</tr>
<tr>
<td>7</td>
<td>160.58</td>
<td>194.87</td>
</tr>
<tr>
<td>8</td>
<td>171.82</td>
<td>214.36</td>
</tr>
<tr>
<td>9</td>
<td>183.85</td>
<td></td>
</tr>
<tr>
<td>10</td>
<td>196.72</td>
<td></td>
</tr>
<tr>
<td>11</td>
<td>210.49</td>
<td></td>
</tr>
</tbody>
</table>
Value Approaches

Now that we have covered the foundational concepts, let’s examine methods for determining investment value.

Real estate professionals know that the #1 question from buyers and sellers is, “What is the value of the property?” Investors want to know if the income from a property will achieve the desired return on investment.

Let’s take a look at three approaches for determining property value:

- **Sales**
- **Cost**
- **Income**

The choice of approach depends on the type, size, and complexity of a property as well as the buyer’s objectives. A combination of methods may be used to fully analyze and confirm the investment value of a property. Using multiple methods usually necessitates further analysis to reconcile outcomes.

**Sales Approach**

The sales approach for determining value is quite familiar to residential practitioners because it is the method most commonly used for single-family homes and small properties. The sales approach compares actual current sales of similar properties, commonly known as a comparative market analysis (CMA). Adjustments may be made for the individual features of the property.

**Cost Approaches**

Cost approaches focus on the price tag for reconstructing the property on vacant land. It can be the best approach for determining the value of a very new building, one that lacks comparables, or a unique or historic building. Value determination based on cost is calculated by subtracting the physical, functional, and economic depreciation (not depreciation for adjusted tax basis) from the price for reproducing or replacing the structure and adding in the value of the vacant land.
Cost approach valuation methods are:

- **Reproduction**: duplication of the current structure
- **Replacement**: reconstruction of a similar structure using current materials and methods, and updating structural components. Replacement costs are usually calculated in one of the following ways:
  - **Comparison cost per square foot**: this method uses construction costs per square foot of similar recently developed properties. The comparative cost is multiplied by the structure’s square footage using the external dimensions. This approach is effective when there are other standardized properties for comparison.
  - **Segregated costs**: Also referred to as unit-in-place, this approach adds together the cost of all of the components including materials, labor, and overhead.
  - **Quantity survey**: this approach estimates the separate costs of materials, labor, and other construction elements.
  - **Index**: Although probably the least accurate, an index approach produces a ballpark estimate by increasing the actual construction cost by a percentage for price increases for labor and materials.

**Income Approaches**

Investors value and purchase properties based on the income stream—from apartment buildings, office space, retail, malls, and the like—and appreciation potential. Therefore, value determinations based on potential income are important and resonant indicators. We will take a look at these commonly used income approaches:

- Gross rent multiplier
- Net operating income (NOI) and cash flow
- Income capitalization
- Cash on cash (ConC)
- Net present value
- Internal rate of return (IRR)
**Gross Rent Multiplier (GRM)**

The GRM is an easy calculation for evaluating small income properties and comparing similar properties. Values and rental income from similar properties can be used as a comparative GRM. Valuation by GRM does not adjust for expenses or factors such as location and property condition.

\[
\text{Sales price} \div \text{potential rental income (PRI)} = \text{GRM}
\]

With the GRM calculation, PRI is typically for one year. Let’s look at an example.

**Example**

A property that is priced at $450,000 has a monthly PRI of $1,500 from each of 4 apartments.

\[
\text{GRM} = \frac{\text{Sale Price}}{\text{one-year PRI}}
\]

\[
\text{GRM} = \frac{450,000}{(1,500 \times 4 \text{ apartments} \times 12 \text{ months})}
\]

\[
\text{GRM} = \frac{450,000}{72,000}
\]

\[
\text{GRM} = 6.25
\]

**Net Operating Income (NOI) and Cash Flow**

Income-based approaches analyze the value of the income stream and project current and future value. In order to perform these calculations, the practitioner must have access to information on the income and expenses, known as net operating income (NOI), and the cash flow over a period of several years.

**NOI**

Net operating income (NOI) is a “snapshot” of a property’s financial performance at a specific date. Gross operating income is figured by subtracting allowances for vacancies and credit losses from the total potential rental income (PRI) and adding any other income. Vacancy and credit losses are usually presented as a percentage of PRI.
NOI is usually presented as a before-tax figure and therefore does not factor in depreciation or value appreciation.

**Gross Potential Rental Income (PRI)**
- Vacancy and Credit Losses
+ Other Income
= Gross Operating Income
- Expenses
= Net Operating Income (NOI)

**Example**

<table>
<thead>
<tr>
<th>Gross Potential Rental Income (PRI)</th>
<th>$115,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Vacancy and Credit Losses</td>
<td>9,900</td>
</tr>
<tr>
<td>+ Other Income</td>
<td>700</td>
</tr>
<tr>
<td>= Gross Operating Income</td>
<td>105,800</td>
</tr>
<tr>
<td>- Expenses</td>
<td>22,300</td>
</tr>
<tr>
<td>= Net Operating Income (NOI)</td>
<td>83,000</td>
</tr>
</tbody>
</table>

**Cash Flow**

- **Cash Flow Before Taxes** (CFBT) is figured by subtracting the amount of annual debt service from NOI.

- **Cash Flow After Taxes** (CFAT) is figured by subtracting income tax owed from cash flow before tax.

Data are usually compiled in standard formats known as an Annual Property Operating Data (APOD) form for NOI and a Cash Flow Analysis (CFA). Preprogrammed Excel spreadsheets for both NOI and CFA can be downloaded from Microsoft.com.
Income Capitalization (Income, Rate, and Value)

While NOI is used to estimate the value of a property and help measure its performance, income capitalization is the market valuation of a property based upon a one-year projection of income. In other words, it relies on a single year’s stabilized NOI to estimate the value of a property. The income capitalization approach estimates the value of a property by applying a proper investment rate of return to the annual NOI that the property is expected to produce, using the IRV formula:

\[
\text{Net Operating Income (I) ÷ Capitalization Rate (R) = Value (V)}
\]

The following graphic is useful when thinking of income valuation and the relationship of these variables to one another.

“IRV” is the equation, and the three elements can be flipped to derive each other. For example, this graphic illustrates the following:

\[
\text{NOI (I) ÷ Value (V) = Capitalization Rate (R)}
\]

\[
\text{Capitalization Rate (R) x Value (V) = NOI (I)}
\]

This formula is one of the central tools for understanding the relationship of income to value of the asset. Before we look at some examples using the IRV formula, let's examine some of the terms.

8 Adapted from IREM® course, “Investment Real Estate: Financial Tools” (FIN402)
I = Income = Stabilized NOI

*Stabilized NOI* (I) is the expected earning potential of the property in the absence of undue or extraordinary circumstances. An accurately projected NOI is a critical component in determining value.

R = Capitalization Rate

The *capitalization rate* (R) is a single rate that converts a single year’s income into value. It is often called a cap rate.

- The lower the capitalization rate, the higher the value of the property
- The higher the capitalization rate, the lower the value of the property

Note that any movement down in cap rate is the result of investors willing to pay a higher price for the same income stream. If the cap rate is lower, it means the investor is willing to pay more for the property than its value.

The reverse is also true—when there is a movement up in cap rate it is because investors are not willing to pay as much for a given income stream.
Cap rates can also be used to estimate purchase price and desired NOI.

\[
\text{NOI (Year of Sale)} \div \text{Cap Rate} = \text{Projected Sales Price}
\]

\[
\text{Purchase Price} \times \text{Cap Rate} = \text{Target NOI}
\]

Sources of Capitalization Rates

There are a number of resources available for cap rates. Major buyers of real estate, such as pension funds, real estate investment companies, and life insurance companies, can be contacted for information on cap rates. These companies are good sources for cap rates for large properties. Industry publications and commercial brokers, as well as banks and other lenders, are also good sources for cap rates.

Because markets change, cap rates will fluctuate, in some markets widely, over time. Cap rates indicate value as a snapshot in time. And as you would expect, the capitalization rate varies between properties. Demand for a particular type of property, quality of the property, and future potential benefits are key variables that influence the capitalization rate. For example, a prime shopping center with a strong operating history and an excellent future potential may sell at a 7% capitalization rate, while a small strip center in a less desirable location with lesser quality tenants may sell at a 9.5% capitalization rate to reflect greater risk. Capitalization rates are also influenced by the broader economic cycles, which may put pressures on demand.

You should keep in mind that cap rates change when using market research to establish value, and you should update calculations accordingly. When using market data to establish cap rates, several comparable properties should be used for a representative sample. Even small fluctuations in the cap rate can have a large impact on the resulting value.

Using the IRV Formula

As was mentioned earlier, the IRV formula (Income \(\div\) Rate = Value) can be rearranged to calculate any of its elements: Income (NOI), Cap Rate, or Value. In the following examples, we use IRV to derive cap rate, income, and market value.
**Example: Finding the Cap Rate**

Consider a retail building that was bought for $3.25 million with an NOI of $295,000. Calculate the cap rate (R).

\[
\text{NOI (I) ÷ Value (V) = Cap Rate (R)}
\]
\[
295,000 ÷ 3,250,000 = 9.08\%
\]

The cap rate is 9.08%.

**Example: Finding Income**

Consider an initial value of a townhouse used as a vacation home and a rental in the first year of the investment at $200,000 with a capitalization rate of 7%. Calculate the NOI (I).

\[
\text{Value (V) × Cap Rate (R) = NOI (I)}
\]
\[
\text{First year of investment: } \$200,000 (V) × 0.07 (R) = \$14,000 (I)
\]
\[(\$200,000 × 7\% = \$14,000)\]

The first-year NOI is $14,000.

**Example: Finding Value**

A suburban office building has an NOI of $200,000 and a cap rate of 7%. Calculate the market value.

\[
\text{NOI (I) ÷ Cap Rate (R) = Value (V)}
\]
\[
\$200,000 ÷ 0.07 = \$2,857,142.86
\]
\[(\$200,000 ÷ 7\% = \$2,857,142.86)\]

The owner of this building might expect a selling price of $2,857,142.86.

**Cash on Cash (ConC)**

Cash on Cash (ConC) measures the investor’s desired rate of return on an initial investment. This ratio compares the equity invested in a property with the cash flow, before or after taxes, from one year. It is most commonly used to show year-to-year trends in performance.
Cash on Cash can be expressed in an equation that relates cash flow and initial equity:

\[
\text{Cash Flow ÷ Initial Equity} = \text{Cash on Cash}
\]

Initial equity invested includes the down payment and all acquisition costs that are not financed. The cash-on-cash rate of return measures a one-year return on invested dollars. It is a snapshot of performance and thus does not consider the effects of time on the investment.

**Example**

A client from Thailand is thinking of purchasing a warehouse that will cost a total of $1,000,000. It has an annual NOI of $95,000. The client can get a loan for $800,000 with annual debt service payments of $77,000. The client will put down $200,000.

\[
\text{Cash Flow ÷ Initial Equity} = \text{Cash on Cash}
\]

To calculate Cash on Cash, we must first calculate the before tax cash flow.

\[
\text{Before Tax Cash Flow} = \$95,000 \text{ NOI} - \$77,000 \text{ Annual Debt Service} = \$18,000
\]

\[
\$18,000 ÷ \$200,000 \text{ (down payment)} = 9.0\%
\]

The Cash on Cash for this investor is 9.0%.

**Net Present Value**

Compared to preceding approaches, Net Present Value (NPV) is a more complex but also more accurate analysis of rate of return because it takes into consideration varying cash flows, initial outlay, and sales price.

NPV is calculated by subtracting the present value of future cash flows and sales price discounted by the investor’s desired rate of return from the initial investment. NPV is best used to evaluate a potential investment when the investor’s desired rate of return is known.
The result is a number, not a percentage, which will be greater than, less than, or equal to zero.

- Greater than zero indicates a higher than desired rate of return
- Zero indicates the desired and actual rate of return are equal
- Less than zero indicates a lower than desired rate of return

**Example**

An investor makes an initial outlay of $100,000 for a condominium, which has anticipated varying cash flows over a period of 5 years, as shown in the table below. Projected sales price after 5 years is $180,000. Based on a 12% desired rate of return, the NPV might look like this:

<table>
<thead>
<tr>
<th>Year</th>
<th>Income</th>
<th>PV</th>
<th>NPV</th>
</tr>
</thead>
<tbody>
<tr>
<td>Initial outlay</td>
<td>-100,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Year 1 income</td>
<td>$9000</td>
<td>$8,035.71</td>
<td></td>
</tr>
<tr>
<td>Year 2 income</td>
<td>$10,000</td>
<td>$7,971.93</td>
<td></td>
</tr>
<tr>
<td>Year 3 income</td>
<td>$11,000</td>
<td>$7,829.58</td>
<td></td>
</tr>
<tr>
<td>Year 4 income</td>
<td>-$3,000</td>
<td>-$1,906.55</td>
<td></td>
</tr>
<tr>
<td>Year 5 income</td>
<td>$12,000</td>
<td>$6,809.12</td>
<td></td>
</tr>
<tr>
<td>Year 6 sale</td>
<td>$180,000</td>
<td>$91,193.60</td>
<td></td>
</tr>
<tr>
<td><strong>NPV</strong></td>
<td></td>
<td><strong>$19,933.39</strong></td>
<td></td>
</tr>
</tbody>
</table>

The positive NPV means that the present value of the future cash flows exceeds the cost of the investment and indicates that the investor’s desired rate of return of 12 percent is also exceeded.

**Internal Rate of Return (IRR)**

Internal rate of return discounts the net present value of all cash flows to zero in order to find the actual rate of return. In other words, it is the discount rate at which the present value of an investment is equal to the present value of the cash flow of the investment. IRR is best used when the investor does not have a desired rate of return in mind.
Calculation of both NPV and IRR are complex processes that are best accomplished with a financial calculator or preprogrammed spreadsheet. Financial analysis spreadsheets can be downloaded from the Web site of the CCIM Institute (www.ccim.com).

For Further Study

As mentioned at the beginning of the chapter, a full study of value concepts is beyond the scope of this course. However, there are plenty of resources at your disposal if you would like to learn more.

- **CCIM Institute**: an array of courses on the financial analysis of commercial and investment real estate, including those that are part of the CCIM designation curriculum. Visit www.ccim.com.

- **Institute of Real Estate Management (IREM)**: several courses on financial analysis for investment real estate, including those that are part of the Certified Property Manager® (CPM) curriculum. Visit www.irem.org.

Key Point Review

- The elements of an investment include yield, or rate of return, safety, leverage, and control.

- According to the principle of the time/value of money, the value of a sum of money received today is greater than the value of the same amount in the future.

- Compounding occurs when invested money gains value. Discounting converts future values to present values.

- Opportunity cost is the rate of return that could be achieved by an alternative investment.

- Three approaches for determining property value are: sales, cost and income. The sales approach compares actual current market values of similar properties. The cost approach focuses on the price tag for reconstructing the property on vacant land. Income-based approaches analyze the value of the income stream.

- Income-based valuation approaches include: gross rent multiplier, net operating income and cash flow, income capitalization, cash on cash (ConC), net present value, and internal rate of return (IRR).
The Next Chapter
The formulas presented in this chapter provide tools for evaluating and comparing investments. The next chapter focuses on placing these formulas within a context so that clients and customers can make informed decisions. A systematic approach to synthesizing data about the client and potential investments transforms data into knowledge.

Notes:
GLOBAL REAL ESTATE: TRANSACTION TOOLS

7

COMPILING TRANSACTION DATA FOR DECISION MAKING
In This Chapter

- Six-step transaction preparation process
- Helping clients and customers make informed decisions

How to use the information in this chapter

- Follow a systematic approach to preparing for a transaction
- Identify properties that meet the personal and investment objectives of clients and customers
Six-Step Preparation Process

If you receive a referral for a foreign buyer, how do you begin compiling and synthesizing all of the information needed for a successful transaction? The following six-step template outlines a basic—and flexible—preparation process; as you use this template in day-to-day business, add research items and calculations to complete the picture.

1. Develop a client profile.
2. Convert area and currency (if necessary).
3. Determine investment objectives--financial and nonfinancial.
4. Determine purchase motivations.
5. Assemble a team.
6. Identify what the local market can offer.

Step #1: Develop a Client Profile

- **Name(s)**
  Legal name, nickname, form of address

- **Contact Information**
  Mailing address, phone numbers, fax number, e-mail address, Web site, social media sites

- **Nationality**
- **Citizenship**
- **Tax Home**
  Location of the client’s primary residence or tax home

- **Occupation**
- **Employer**
- **Residency Status**
- **Family Information**
- **Client’s experience and knowledge of market**
- **Cultural Considerations**
  Language, expectations, decision making
Discussion Question
When working with a foreign client or customer, what questions do you ask in order to develop a profile?

Step #2: Convert Area and Currency
✓ Convert currency (See page 44)
✓ Convert area measures (See page 25)

Step #3: Investment Objectives
✓ Stated Requirements
  Type and size of property—residential or commercial/investment, single-family home, condo, office building, retail property, vacation home, retirement residence
✓ Price range
✓ Location and type of funds
✓ Will financing be needed?
✓ Amount of cash the client will apply to the transaction
7. Compiling Transaction Data for Decision Making

- **Anticipated holding period**
- **Financial targets**
  - NOI
  - Cap Rate
  - % Equity or Financing
  - Loan Terms
  - Monthly Loan Payment
  - Cost of Points
  - Transaction Costs
  - ConC Before/After Tax
  - Projected Sales Price
  - Sale Proceeds Before / After Taxes

<table>
<thead>
<tr>
<th>Objective</th>
<th>Property Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income</td>
<td>Retail, office, industrial, land, resorts, apartment buildings</td>
</tr>
<tr>
<td>Development</td>
<td>Land for development, buildings for rehab or redevelopment</td>
</tr>
<tr>
<td>Sheltering capital</td>
<td>Land or net leased properties with credit tenants</td>
</tr>
<tr>
<td>Business</td>
<td>Retail, office, industrial, distribution, farms, mines or woodlots</td>
</tr>
<tr>
<td>Vacation or retirement</td>
<td>Houses, condos or timeshares</td>
</tr>
</tbody>
</table>

**Step #4: Determine Purchase Motivations**

- **Lack of investment opportunities**
  The client’s home economy may lack viable real estate investments or be overbuilt. Excess capital or a restrictive investment and regulatory environment can drive away investment.

- **Protect capital against inflation and other domestic threats**
  Inflation is always a threat to capital. Other threats include currency devaluation, government changes, and nationalization of private real estate holdings and industries.

- **Diversification**

- **Cash flow and profits**

- **Value appreciation**
Global Real Estate: Transaction Tools

- Establish a basis for residency or citizenship
- Expand a business into a foreign market
- Vacation home, retirement residence
- Protect family interests
- Prestige
- Safety, refuge in case of conflict

Discussion Question
What motivates foreign buyers in your market? What questions do you ask to learn a client’s motives?

Step #5: Assemble a Team

The complexities of global transactions require the assistance of other professional specialists. The advice of legal, tax, and financial experts is extremely important. As you build your team, evaluate specialists’ qualifications based on:

- Expertise
- Specialization in commercial or residential transactions
- Experience in global transactions
- References
7. Compiling Transaction Data for Decision Making

- Compatibility with you and your client
- Knowledge of tax laws, property type, zoning requirements, and relevant regulations
- Fee structure—per transaction fee or hourly billing

Discussion Question
What experts should be part of your team?

Step #6: What Can Your Market Offer?

✔ Market Profile
Study your market from a global perspective to understand what it can offer your client. You could use the Country Assessment Model introduced at the beginning of this course (see page 10).
Property Profiles

- Property name
- Tenants
- Location
- Monthly gross rental income and NOI
- Type
- Cap rate and other projections
- Size (buildings, land)
- Cost recovery deduction
- Price
- Income and appreciation potential

Wrap Up

Real estate buyers or sellers from other parts of the world rely on the real estate professional’s guidance and market knowledge to make decisions.

In-depth market knowledge and the ability to apply it for a client’s advantage strengthen the real estate professional’s value proposition and competitive edge. A systematic approach to compiling and evaluating market data provides the knowledge base.

Because foreign buyers, such as investors and vacation-home buyers, compare areas as well as properties, you should have ready answers to how your market compares to others.
Resources

Web Sites .................................................................................................................. 123
Currency Unions ....................................................................................................... 125
Glossary .................................................................................................................... 126
<table>
<thead>
<tr>
<th><strong>Web Sites</strong></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>NATIONAL ASSOCIATION OF REALTORS®</td>
<td><a href="http://www.Realtor.org">www.Realtor.org</a></td>
<td>eXchangeRate.com</td>
</tr>
<tr>
<td><a href="http://www.Realtor.org">www.Realtor.org</a></td>
<td></td>
<td><a href="http://www.exchangerate.com">www.exchangerate.com</a></td>
</tr>
<tr>
<td>NATIONAL ASSOCIATION OF REALTORS®</td>
<td><a href="http://www.Realtor.org/global">www.Realtor.org/global</a></td>
<td>FIABCI International Real Estate Federation</td>
</tr>
<tr>
<td>Commercial and Global Services</td>
<td></td>
<td><a href="http://www.fiabci-usa.com">www.fiabci-usa.com</a></td>
</tr>
<tr>
<td><a href="http://www.Realtor.org/global">www.Realtor.org/global</a></td>
<td></td>
<td>Google Translate</td>
</tr>
<tr>
<td>NATIONAL ASSOCIATION OF REALTORS®</td>
<td><a href="http://www.Realtor.org/research-and-statistics">www.Realtor.org/research-and-statistics</a></td>
<td><a href="http://www.google.com">www.google.com</a> (click on more)</td>
</tr>
<tr>
<td>Realtors Property Resource®</td>
<td></td>
<td>HiFx Currency Converter</td>
</tr>
<tr>
<td><a href="http://www.narrpr.com">www.narrpr.com</a></td>
<td></td>
<td><a href="http://www.hifx.com">www.hifx.com</a></td>
</tr>
<tr>
<td>NATIONAL ASSOCIATION OF REALTORS®</td>
<td><a href="http://www.Realtor.org/research-and-statistics">www.Realtor.org/research-and-statistics</a></td>
<td>International Real Property Foundation</td>
</tr>
<tr>
<td>Research &amp; Statistics</td>
<td></td>
<td><a href="http://www.irpf.org">www.irpf.org</a></td>
</tr>
<tr>
<td>NAR Economists’ Outlook</td>
<td><a href="http://economistsoutlook.blogs.realtor.org">http://economistsoutlook.blogs.realtor.org</a></td>
<td>MSN Money Currency Converter</td>
</tr>
<tr>
<td>NAR and REBAC course schedules</td>
<td><a href="http://www.training4RE.com">www.training4RE.com</a></td>
<td><a href="http://investing.money.msn.com/investments/">http://investing.money.msn.com/investments/</a></td>
</tr>
<tr>
<td>Association for Foreign Investors in Real Estate</td>
<td><a href="http://www.AFIRE.org">www.AFIRE.org</a></td>
<td>currency-converter-calculator</td>
</tr>
<tr>
<td>CCIM Institute</td>
<td><a href="http://www.ccim.com">www.ccim.com</a></td>
<td>Online Conversion</td>
</tr>
<tr>
<td>CoinMill.com</td>
<td><a href="http://coinmill.com">http://coinmill.com</a></td>
<td>U.S. Bureau of Economic Analysis</td>
</tr>
<tr>
<td>Economist Forecasts</td>
<td><a href="http://www.economist.com/theworldin">www.economist.com/theworldin</a></td>
<td>U.S. Department of Agriculture, Farm</td>
</tr>
<tr>
<td>Exchange rates and exchange rate history</td>
<td><a href="http://www.exchange-rates.org">www.exchange-rates.org</a></td>
<td>Service Agency</td>
</tr>
<tr>
<td></td>
<td></td>
<td><a href="http://www.fsa.usda.gov">www.fsa.usda.gov</a></td>
</tr>
<tr>
<td></td>
<td></td>
<td>U.S. Department of Homeland Security</td>
</tr>
<tr>
<td></td>
<td></td>
<td><a href="http://www.dhs.gov">www.dhs.gov</a></td>
</tr>
<tr>
<td></td>
<td></td>
<td>U.S. Department of Housing and Urban</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Development</td>
</tr>
<tr>
<td></td>
<td></td>
<td><a href="http://www.hud.gov">www.hud.gov</a></td>
</tr>
<tr>
<td></td>
<td></td>
<td>U.S. Internal Revenue Service</td>
</tr>
<tr>
<td></td>
<td></td>
<td><a href="http://www.irs.gov">www.irs.gov</a></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Universal Currency Converter</td>
</tr>
<tr>
<td></td>
<td></td>
<td><a href="http://www.xe.com">www.xe.com</a></td>
</tr>
</tbody>
</table>
Yahoo Finance Currency Converter
http://finance.yahoo.com/currency-converter

World Lingo Translation
www.WorldLingo.com

World Clock
www.timeanddate.com/worldclock

XE (exchange rates)
www.xe.com
## Currency Unions

### The Euro Zone

<table>
<thead>
<tr>
<th>Country</th>
<th>Country</th>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Andorra *</td>
<td>Greece</td>
<td>Netherlands</td>
</tr>
<tr>
<td>Austria</td>
<td>Ireland</td>
<td>Portugal</td>
</tr>
<tr>
<td>Belgium</td>
<td>Italy</td>
<td>San Marino *</td>
</tr>
<tr>
<td>Cyprus</td>
<td>Kosovo *</td>
<td>Slovakia</td>
</tr>
<tr>
<td>Estonia</td>
<td>Luxembourg</td>
<td>Slovenia</td>
</tr>
<tr>
<td>Finland</td>
<td>Malta</td>
<td>Spain</td>
</tr>
<tr>
<td>France</td>
<td>Monaco *</td>
<td>Vatican City *</td>
</tr>
<tr>
<td>Germany</td>
<td>Montenegro *</td>
<td>* Non EU countries</td>
</tr>
</tbody>
</table>

### Central and West African Franc

#### West Africa

<table>
<thead>
<tr>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Benin</td>
</tr>
<tr>
<td>Burkina Faso</td>
</tr>
<tr>
<td>Côte d’Ivoire</td>
</tr>
<tr>
<td>Guinea-Bissau</td>
</tr>
<tr>
<td>Mali</td>
</tr>
<tr>
<td>Niger</td>
</tr>
<tr>
<td>Senegal</td>
</tr>
<tr>
<td>Togo</td>
</tr>
</tbody>
</table>

#### Central Africa

<table>
<thead>
<tr>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cameroon</td>
</tr>
<tr>
<td>Central African Republic</td>
</tr>
<tr>
<td>Chad</td>
</tr>
<tr>
<td>Republic of the Congo</td>
</tr>
<tr>
<td>Equatorial Guinea</td>
</tr>
<tr>
<td>Gabon</td>
</tr>
</tbody>
</table>

### East Caribbean Dollar

<table>
<thead>
<tr>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Anguilla</td>
</tr>
<tr>
<td>Antigua and Barbuda</td>
</tr>
<tr>
<td>Dominica</td>
</tr>
<tr>
<td>Grenada</td>
</tr>
<tr>
<td>Montserrat</td>
</tr>
<tr>
<td>St. Kitts and Nevis</td>
</tr>
<tr>
<td>St. Lucia</td>
</tr>
<tr>
<td>St. Vincent and the Grenadines</td>
</tr>
</tbody>
</table>
## Glossary

### A

**Adjusted basis**
A base price from which to evaluate the gains or losses incurred upon the sale of an asset. The basis is determined by adding the value of capital improvements to the original price of the property, and subtracting cost recovery deductions.

**Amortize**
The gradual elimination of a liability, such as a mortgage, in regular payments over a specified period of time.

**Annual debt service (ADS)**
The total amount of principal and interest paid each year.

### B

**Basis**
The price an investor pays for an asset; used to determine capital gain or loss for tax purposes.

### C

**Capital flow**
The movement of money, people, skills, and ideas across national boundaries in exchange for other goods or services.

**Capitalization rate (cap rate)**
A ratio that represents the future income of an income-producing property.

**Cash flow before taxes (CFBT)**
Net operating income less annual debt service.

**Cash on cash (ConC)**
A measure of yield on an investment, calculated by dividing cash flow before or after tax by the original investment amount.

**Compounding**
A process used in calculating the time value of money to determine the future value of an investment.

**Cost Approach**
A method for valuing property that uses the cost for duplicating or replacing the same structure on vacant land.

**Cost recovery**
Depreciation. A deduction from taxable income based on the economic life of an asset.

**Currency union**
A group of countries that agree to use a common currency.

### D

**Debt coverage ratio (DCR)**
Ratio of net operating income (NOI) to annual debt service. It is determined by dividing NOI by annual debt service (or mortgage payment).

**Depreciation**
Cost recovery. Annual tax deduction allowed to compensate for the declining economic value of an asset.

**Discounting**
The present value (PV) of money to be received in the future; reduced to reflect the opportunity cost of waiting to receive the money.
Dollarization
Substitution, formalized or *de facto*, of one country’s currency for another.

**E**

EIN—Employer Identification Number
A tax identifier issued by the IRS to a foreign corporation.

Equity
The amount of cash invested; loan amount less down payment.

Exchange rate
The value of one currency in terms of another; the amount of one currency equivalent to another.

**F**

Fèng shui
A Chinese belief system based on creating harmony between humans and the environment by placement of dwellings, buildings, room arrangements, and so forth. Also known as geomancy.

FIRPTA—Foreign Investment in Real Property Act
U.S. law requiring the buyer of a U.S. property interest from a foreign seller to withhold 10 percent of the purchase price and remit it to the IRS within 20 days of closing.

Fixed exchange rate
An exchange rate that is officially controlled, or pegged, by the issuing country instead of determined by the world currency market conditions.

Foreign national
A foreign citizen who is present in another country.

Future value
The value of a present sum of money at some point in the future.

Globalization
The trend by countries, companies, organizations, and people toward a single worldwide market environment.

Gross Rent Multiplier
A number calculated by dividing sales price by monthly rents and used for comparing investment value of rental properties.

**H**

Hard currency
A currency that trades on global markets and is viewed by investors as a safe store of capital. Includes U.S. dollar, euro, Swiss franc, U.K. pound, Japanese yen, Swedish krona, Canadian dollar, Norwegian krone, Australian dollar, New Zealand dollar, and gold.

Hectare
A metric measure for land, equivalent to 2.4710 acres.

**I**

Income Approach
Valuation methods focusing on evaluation of an investment property’s income stream.
Internal rate of return (IRR)
The discount rate at which the present value of the future cash flows of an investment equals the cost of the investment itself. An investment is considered acceptable when the IRR yield is greater than the required rate of return.

Internal Revenue Service (IRS)
The federal government entity that regulates and enforces tax laws in the USA.

IRV formula
A formula used to calculate value, return, or income.

Leverage
The use of borrowed funds to finance an investment.

Loan to value (LTV)
The amount of money borrowed compared to the total value of a property. It is determined by dividing the amount of the loan by the property value.

Managed float
A floating exchange rate plan in which fluctuation within a set range is allowed but a government may intervene to influence the exchange rate by buying or selling currency.

Net Present Value
The difference between the cost of a real estate investment and the discounted present value of anticipated future fiscal benefits of that investment.

NOI—Net operating income
Income from an investment after subtracting vacancy losses and operating expenses.

Non-quantitative motivations
Investor objectives based on personal preferences.

Non-resident alien
A foreign citizen who is granted entry to but does not reside in the USA.

Opportunity cost
The rate of return that could be earned on an alternative investment. Rate of return lost due to lack of investment.

Physical presence
For tax purposes, presence in the USA for more than 30 days but fewer than 183 days.

Potential rental income (PRI)
Amount of rental income received if 100 percent of rental units are leased.

Present value
The value of a future sum, discounted to reflect the time value of money.

Quantitative motivations
Investor objectives that are tied to the pursuit of profit and investment gains.
R

Repatriation
Return of capital or people to the country of origin.

Resident alien
A foreign citizen who is granted legal residence.

Risk
A measure of the probability of gains or loss in the value of an investment.

S

Sales Approach
Method for valuing property by comparing it to prices for similar properties.

7/10 rule
Rule of thumb for length of time and interest rate necessary for an investment to double—7 years at 10 percent, 10 years at 7 percent.

Soft currency
A foreign currency generally not viewed or held by investors as a store of capital.

Substantial presence
Presence in the United States for a weighted average of 183 days over a three-year testing period.

T

Tax home
The area (city, state, country) of a taxpayer’s main place of business or employment.

Tax treaty
An agreement between countries for the purpose of preventing double taxation.

Time value of money (TVM)
An economic principle that states that the present value of money is greater than a similar sum in the future.

TIN—Taxpayer Identification Number
An identifier issued by the IRS to an individual who does not qualify for a Social Security Number. Required for foreign real estate buyers.

V

Vacancy loss
A percentage of potential rental income, deducted to account for losses due to unoccupied rental units.

Y

Yield
The measure of return on an investment.