Chapter 16 Multiple Choice Questions

1. Which of the following is not normally included as one of the advantages of real estate as an investment?
   a. Liquidity
   b. Cash flow from operations
   c. Possible appreciation in value
   d. Diversification opportunities

2. The term _______ refers to principal and interest payments for any outstanding mortgage debt.
   a. debt service
   b. BTER
   c. ATER
   d. NOI

3. The term _______ refers to the cash flow a real estate investor can put in his or her pocket at the end of the year.
   a. NOI
   b. ATER
   c. BTER
   d. leverage

4. The term _______ refers to the process of spreading risk exposure across different investment opportunities.
   a. diversification
   b. leverage
   c. depreciation
   d. appreciation

5. The deduction of tax depreciation from taxable income tends to _______ the capital gains upon sale of the property.
   a. reduce
   b. increase
   c. have no effect upon
   d. defer
6. Under current tax law, nonresidential investment real estate has a depreciable life of _______ years, and residential investment real estate has a depreciable life of _______ years.
   a. 27.5, 49  
   b. 31.5, 27.5  
   c. 39, 27.5  
   d. 15, 40

7. Under the current tax law, residential real estate investments have a depreciable life of _______ years.
   a. 27  
   b. 39  
   c. 27.5  
   d. 31.5

8. The internal rate of return is that discount rate at which
   a. the future worth of present cash flow is exactly equal to the initial cash investment.
   b. the present value of future cash flows is larger than the initial cash investment.
   c. the future worth of cash flow is larger than the initial cash investment.
   d. the present value of future cash flow is exactly equal to the initial cash investment.

9. In a cash-flow projection, the net operating income is determined by starting with the gross potential income, calculating the gross effective income, and then
   a. deducting vacancies and bad debts.
   b. deducting depreciation.
   c. deducting operating expenses.
   d. adding depreciation.

10. In a cash-flow projection, the taxable income is determined by starting with the gross potential income, calculating the gross effective income and the net operating income and then
    a. deducting vacancies and bad debts.
    b. adding depreciation.
    c. deducting depreciation.
    d. deducting depreciation and interest expenses.
The following information applies to the next two questions:

Net Operating Income: $14,000
Depreciation: $4,000
Debt Service: $13,000 (interest is $12,000 of this amount)
Vacancy and Credit Loss: $7,000
Interest Expense: $12,000
Operating Expenses: $3,000
Tax rate: 28%

11. Assuming that the investor can use any tax shelter benefits, what are the taxes due or the taxes saved (in $) for these annual figures?
   a. ($1,440)
   b. $560
   c. ($560)
   d. $1,440

12. Assuming that the investor can use any tax shelter benefits, what is the cash flow after taxes?
   a. ($2,000)
   b. $1,000
   c. ($1,440)
   d. $1,560

The following information applies to the next two questions:

Gross Selling Price: 1,000,000
Net Selling Price: $950,000
Accumulated Depreciation: $200,000
Loan Payoff: $350,000
Purchase Price: $350,000
Depreciated Value: $150,000
Capital Gain Tax Rate: 20%
Tax Rate on Capital Gains Due to Depreciation 25%

13. What are the taxes due on the sale?
   a. $50,000
   b. $120,000
   c. $170,000
   d. $280,000
14. What is the ATER?
   a. $430,000
   b. $600,000
   c. $480,000
   d. $550,000

15. According to the net present value decision rule, an investor who is considering a project which has a net present value of $1 would
   a. reject the investment.
   b. lose more money on the investment.
   c. accept the investment.
   d. be indifferent between accepting or rejecting the investment.

16. Which of the following investment analysis measures gives the investor the best measure for overall financial decision making?
   a. Cash on cash return
   b. Income capitalization rate
   c. Net present value
   d. Payback period

17. Negative leverage occurs when the return on equity of the project _______ with the use of _______.
   a. increases, debt
   b. decreases, debt
   c. increases, equity
   d. decreases, debt

18. A person who chose to wealth maximize will choose investments that offer _______ benefits in comparison to costs.
   a. less
   b. greater
   c. equal
   d. no

19. An office building is determined to have a cost of $15,000,000 for depreciation. What is the depreciation amount for the first year if the building was purchased on January 1st?
   a. $384,615
   b. $522,727
   c. $368,590
   d. $545,454
20. An apartment building with a depreciable value of $10,000,000 is purchased on January 1st. What is the depreciation amount for the first year?

a. $363,636  
b. $245,726  
c. $256,410  
d. $348,485