Excerpt from
***Introduction to Real Estate Finance and Investment: Sample Problems, Student Edition*, by Frank Gallinelli**

Chapter 7: Vacancy and Credit Loss Allowance

As the problems in the previous section make abundantly clear, not every residential unit or every square foot of commercial space stays occupied one hundred percent of the time. Or, if it does, then people are giggling behind your back because your rents are so low you couldn't get your tenants to budge with a stink bomb.

It is fair to presume that your perfect-world Gross Scheduled Income will be depleted by vacancy loss. It may also be reduced by something called credit loss, which is a polite term for those individuals or businesses who do indeed occupy your property but somehow fail to pay you for that privilege.

In the current or a past year you might report your loss as the actual dollar amount you experienced. If you are making projections regarding your property's performance in the future, then in most cases you will estimate your loss as a percentage of the property's Gross Scheduled Income. When you do so, you typically call it something like Vacancy and Credit Loss Allowance to indicate that it is indeed an allowance, a cushion to deal with the probability of lost income. In that case, the formula is simply

> **Vacancy and Credit Loss Allowance = Gross Scheduled Income x estimated % vacancy and credit loss**

Problem 7-1:

For the property described in Problem 6-4, what is your vacancy loss percentage?

Problem 7-2:

You own a building with 15 units. Last year, they were all occupied, renting for $600 per month. This year, you expect your Gross Scheduled Income to increase by 2%, but you also project a 3% vacancy and credit loss. If you are right, what will the dollar amount of your vacancy and credit loss be?

Problem 7-3:

In the scenario of Problem 7-2, suppose the fair market rent for your units is \$640 per month. Suppose this year, 14 of the units remain occupied, renting for \$610 per month, while the remaining unit is vacant for 4 months, then rents for the rest of the year at \$640 per month. What will your vacancy loss percentage be this year?

Problem 7-4:

In the scenario of Problem 7-3, suppose one of your tenants at \$610 per month disappears and never pays you the rent for December. What will your vacancy and credit loss percentage be?