

**Real Estate**



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## **Self-Directed IRAs - Investing Retirement Funds in Real Estate**

The key to self-direction is the flexibility to place any legal investment in your Plan, including real estate. Purchasing real estate in your Plan provides investors a hard asset to counterbalance the retirement portfolio traditionally dominated by financial securities. It also allows real estate investors the ability to invest in an asset that they know and understand.

Tax law changes in 2002 significantly enhanced the number of choices and flexibility of self-directed tax-free and tax-deferred plans. This includes new opportunities to consolidate and control investments in fewer accounts as well as the potential to make larger contributions to the qualified retirement plans. This applies specifically to self-employed persons and those with small corporations. Most real estate professionals are in this category. Individuals with SEP retirement accounts will find significant benefits from the new individual 401(k) plans. Among the benefits are contribution limits and flexibility.

Key to self-directing retirement funds to real estate is to have a plan that allows true self direction. Many financial institutions, while promoting self-direction, allow only financial securities to which the institution has easy access or from which it earns commissions. Truly self directed plans allow you the investor to select the investment on your own. Self-directed plan administrators may be located easily via an Internet search. Our organization, Entrust Administration, is currently establishing a network of local affiliate offices to provide investors education and hands-on assistance in self-directing their plan.

Once your Plan or Account is established, you may direct your plan administrator to purchase for your Plan whatever real estate property you choose, within IRS guidelines.

The administrator will not provide investment advice regarding the purchase, they only perform the actions that you direct. The admin-

istrator, following your instructions, reviews documents, signs purchase and other documents on behalf of your Plan.

You may have your Plan partner with other plans or other individuals to make a purchase. You are allowed to finance a portion of the price if you wish. Your Plan may invest in a partnership or LLC that is purchasing real estate. The choice is yours. The ability to put your retirement funds into an investment that you can see, select, control and understand is the power of Self-Direction.

As with any IRS-related pronouncement, there are exceptions. When purchased, the property becomes an asset of your Plan or account. In addition:

- You may not personally own the property purchased by your Plan
- You must ensure that your intended purchase is not a prohibited transaction. A prohibited transaction involves the improper use of your IRA or Qualified Plan holdings by you or any disqualified person. A disqualified person is any member of your immediate family (except siblings), employers, certain partners, fiduciaries, and other categories specified in the IRS code
- It must be for investment purposes only.
- Neither you, your spouse, nor your family members, other than siblings, may have owned the property prior to its purchase by your Plan.
- Neither you nor your family members (other than siblings) may live in or lease the property while it's in your Plan.
- Your business may not lease or be located in or on any part of the property while it's in your Plan.

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## **Self-Directed IRAs - Investing Retirement Funds in Real Estate - cont.**

If you elect to take advantage of debt financing to make the purchase, you should be aware of Unrelated Business Income Tax (UBIT), basically, UBIT is tax on the income produced by the debt financed portion of your investment. Your plan administrator will be able to direct you to appropriate information regarding the UBIT calculation for your proposed purchase.

Once the property is purchased, all the expenses and debt service payments will have to be paid through your Plan. You must make sure that there are sufficient funds available in the Plan on an ongoing basis. If you prefer, you may can hire a management company to receive the rents and pay the bills, or you can arrange for those functions to be handled by the Plan administrator.

If you decide to sell the property, once again you direct the administrator to complete the transaction upon your direction. The proceeds from the sale are put back into your Plan. The administrator can also be directed to distribute the property to you, in part or in whole as a distribution from the plan. This option is a favorite for investors who wish to personally use property in the Plan, such as a retirement home, once they reach the age of 59 1/2.

Real estate in retirement accounts is not a new idea, Entrust has been providing self-directed IRAs since 1981. IRAs have been promoted primarily by financial services companies who do not have the expertise to provide truly self directed plans and whose financial motivations do not provide incentive for the development of such programs. Today, the advent of the Internet is making companies like Entrust more accessible to the average investor and the idea is spreading quickly.