



Steven Finlay, REALTOR® Broker Associate
ABR, CRS, GRI, e-PRO

Serving Green Bay, De Pere, Howard/Suamico, Ashwaubenon, Allouez and Wrightstown
Office: 920.593.4122 | Cell: 920.471.6040 | Fax: 888.427.1359 | Email: realestate@stevenfinlay.com

"Real Estate is my profession, helping people to achieve their goals is my job..."

Use your IRA to Invest in Real Estate

By Tom Lundstedt, CCIM

A short, middle-aged woman wearing red glasses came up to me after one of my real estate seminars. She seemed shy and hesitant, but she'd listened intently and taken lots of notes during the class. She told me her name was Norma and proceeded to ask me several good questions about real estate investing. She happened to mention she had \$200,000 in her retirement account. When I congratulated her, she said, "Don't be impressed. I had \$300,000 a few years ago!"

Her retirement account, like many others, had suffered as a result of investment choices. Norma went on to tell me she wished she had bought real estate instead of "investing in an IRA." She was amazed when I told her she could have her cake and eat it too – or rather, have her IRA and real estate too! Let me explain.

First and foremost: A retirement account (traditional IRA, Roth IRA, SIMPLE IRA, SEP, Keogh, 401K, etc.) is not an investment! It's simply a special account that holds your investments. It can hold many types of investments, such as mutual funds, stocks, bonds, and...drum roll, please: real estate!

Picture a truck with the words "MY RETIREMENT ACCOUNT" painted on the doors. In the back of the truck, you load whichever allowable investments you choose. As you picture this, as yourself, "Is my retirement truck on the way to becoming a big, heavy-duty monster truck, or will I end up with a little, wimpy mini pickup?"

When I told Norma her retirement account *could* own real estate she said, "But I asked the company that administers my account if my IRA could own real estate, and they said 'no.'"

Whoa! Instead of merely saying "no," the person with whom she talked should have added three important words: "not with us." The problem is that most companies that hold retirement accounts aren't geared up to handle real estate. Therefore, they have no incentive to inform their customers that real estate is

an alternative investment choice. That's the main reason for the misconception that real estate can't be held in a retirement account.

Let's get this straight: Retirement accounts can own real estate.

In a minute, we'll get to the basic ins and outs of real estate IRAs. But first some advice: This article is designed to be a launching pad for readers to begin their exploration of real estate IRAs. It's a complicated subject and everyone's situation is unique, so be sure to talk with your competent advisors before you take any action. OK, here we go.

First, establish a self-directed retirement account with a company/custodian that specializes in real estate IRAs. This is a relatively easy process and can be done by either establishing a new account or rolling over the assets of an existing account. (Be sure there are no surrender charges for rolling over an existing account.)

Once you're the proud owner of a self-directed IRA with a custodian that can handle real estate, what's next? There are specific rules as to what you can and cannot do with your real estate IRA.

Some Things You Can Do

1. Your real estate IRA can buy and sell many types of real estate including raw land, rental properties, condos, fixer-uppers, commercial properties, lakeshore, etc.

Keep in mind it's the self-directed real estate IRA that buys, owns and sells the property. Not you personally. You don't withdraw the money from the IRA to buy the property – the custodian buys the property in the name of your self-directed real estate IRA.

2. The property can be rented but the rental income is paid into your IRA, not to you.

3. All the expenses of renting and operating the property must flow in and out of your self-directed real estate IRA.

Be sure your self-directed real estate IRA has enough liquid reserve funds to cover operating expenses, improvements, etc.

4. It is possible to finance a property that is owned by your IRA. But the financing must be “non-recourse.” That means the property, not the IRA account, is the sole security for the loan. Most traditional lenders won’t provide non-recourse financing. However, seller financing or private loans are possibilities. Let me emphasize again: Get good professional advice before taking any action.

5. Your real estate IRA can buy a partial interest in a property. This is useful if your IRA doesn’t have enough money to buy 100 percent of the property. It could be a partner and own a fractional interest.

Some Things You Cannot Do

1. Your real estate IRA cannot buy a property that you, your spouse or certain family members already own. Likewise, your real estate IRA cannot sell a property it owns to you, your spouse or certain family members.

2. You, your spouse or certain family members cannot have any personal use of the property owned by your real estate IRA.

3. Your IRA cannot lease the property to your business. Your business cannot use or occupy any part of the property.

Is a Real Estate IRA Right for You?

So, now you know you *can* use your retirement account to buy real estate. But the bigger issue is *should* you use your retirement account to buy real estate? The answer is, it depends on the type of real estate and your unique situation.

You already know your real estate IRA cannot own property that is used by you, certain family members or your business. Therefore, primary residences, second homes and vacation homes are not candidates.

In addition, a rental property that produces tax shelter from depreciation deductions would probably not be a good fit because the tax shelter would go to waste in your retirement account.

Other types of real estate, such as raw land, fixer-uppers, and non-leveraged rental properties, are perfect candidates. The profit from these investments would be taxed if you owned the property personally. However, if your real estate IRA buys, owns and sells the property, the profit would compound in your IRA tax-deferred (or tax-free if it’s a Roth IRA)!

Keep in mind, there is a limit on how much you can contribute each year to your retirement account. But, there’s no limit on how much the account can earn! Hubba Hubba!

Last But Not Least

1. Before your IRA buys any property, you’ve got to understand how real estate works. There’s a lot to it. Make a commitment to learn how to analyze a property before you buy it, including operating expenses and management considerations. Study the financial benefits such as cash flow, depreciation and appreciation. Learn how to determine cap rates, cash on cash and other rates of return. And so on. The more you know, the better your chance of success.

2. Remember that real estate IRAs are a specialty and not every retirement account administrator/custodian is geared up to handle them. In the “Future Resources” box I’ve included several real estate IRA custodians (as well as some other resources) to get you started. Bear in mind, there are other custodians and you need to find one that’s right for you. Check out their web sites or call them.

Finally, if the choices you’ve made so far for your retirement account aren’t taking you where you want to go, find a new vehicle. Real estate opportunities are everywhere for those savvy enough to recognize them and motivated enough to take action.

What a country!

Further Resources

Entrust	1-800-392-9653	www.entrustadmin.com
Lincoln Trust	1-800-825-2501	www.lincolntrust.com
Sterling Trust	1-800-955-3434	www.sterling-trust.com

- On the Internet, enter “real estate IRA” on a search engine such as Google
- Another good resource is the book, *IRA Wealth*, by Patrick W. Rice with Jennifer Dirks
- For more information on buying, owning and selling investment real estate, visit the “Products section at www.tomlundstedt.com

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