

POTTS FINANCIAL SERVICES

Published In *Condo Owner, Florida and Alabama* Issue, Fall 2003

Using Your IRA To Purchase Real Estate

By Alan N Potts

Many people today are questioning their investment decisions, the integrity of our financial markets and our rules of law. This can be attributed, in part, to the financial fiascos of Enron, WorldCom, Xerox, Sunbeam and Imclone, just to name a few. Questionable accounting practices, bonanza executive stock options and special corporate loans make people question the validity of our “free market” system.

Warren Buffet, recognized as one of the richest men in the world, in an interview with *Outstanding Investor Digest*, said, “I think stocks are a decent way to make 6 to 7 percent per year over the next 15 to 20 years. But I think anybody who expects to make 15 percent per year-or expects their broker or investment advisor to make that kind of money-is living in a dream world.” Based on Buffet’s statement, ask yourself this: are stocks and mutual funds the right place for your money?

According to the Investment Company Institute Research “there are approximately \$2 trillion invested in IRAs (Individual Retirement Accounts).” Mutual fund companies, stock brokerage firms, banks and other financial institutions hold the majority of these accounts.

Many investors monitor their IRAs regularly and have become very familiar with their performance, but most people do not know they can use their IRA monies to purchase real estate, including rental condominiums.

It’s a fact that an IRA can be used to purchase real estate, and there are two ways the transaction can be completed. The real estate can either be purchased “inside” and owned by the IRA, or the real estate can be purchased “outside” the IRA and owned outright. Owning real estate inside an IRA is considered a non-traditional approach; owning real estate outside an IRA is considered a more traditional approach. Let me explain.

If you purchase real estate and place the property inside your IRA, you do not own it; your IRA owns the property. Since qualified plan law governs your IRA, the owner must adhere to Internal Revenue Service guidelines. Investment restrictions, custodial fees, distribution rules and, ultimately, income taxes must be paid. All proceeds must go back into the IRA and occupancy is not an option. In addition, if the real estate is a rental property, for compliance purposes, your custodian will appoint a property manager. If loans are used, the loan must be a nonrecourse loan (secured by the property but no recourse on any other assets). Commercial lenders usually do not engage in these types of loans, so the private sector (private investors, owner/seller financing, etc.) is your best option

The second way an IRA owner can use an IRA to purchase property is for the real estate to be purchased outside the IRA and owned outright. This approach is more traditional because the individual owns the real estate and therefore holds title. Since the individual owns the real estate, real estate law governs the owners investment. Real estate law is more consumer friendly, and the real estate can qualify for long-term capital gains income tax treatment and many other financial and economic benefits. Depreciation, additional write-offs, income flexibility and a stepped-up income tax basis are possible. The use of 1031 Tax Deferred Exchanges and/or the Personal Residence Exclusion are now possibilities.

POTTS FINANCIAL SERVICES

Published In *Condo Owner, Florida and Alabama* Issue, Fall 2003

Using Your IRA To Purchase Real Estate

By Alan N Potts

An IRA can completely or partially fund a real estate purchase. In addition, you can purchase and own the property outright or share ownership with other IRA and non-IRA owners.

Many people have not heard that purchasing real estate via an IRA is a possibility and certainly are not aware that there are two possible ways to make this type of purchase. Both approaches have been around for many years, and real estate gives the investor options other than stocks, mutual funds, money markets and certificates of deposit.

Editor's Note: This article is for informational purposes only. Readers are advised to discuss this information with their legal and/or tax advisor in order to gain more knowledge on this topic.