

From the office of **Phil Simone:**

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## Holding Real Estate in an IRA

*Is this unorthodox investment idea underappreciated?*

You can invest your IRA assets in different ways. Should you invest a portion of those assets in real estate?

At first thought, putting real estate into an IRA may seem like an off-the-wall idea. It is one you might want to consider, but you must be aware of the rules. The concept is not new, but it has been slow to gain acceptance. Less than 2% of IRA assets are held in real estate.<sup>1</sup>

**The 2007-09 bear market led some IRA owners to explore alternative investments.** That was when the term “self-directed IRA” entered the investing lexicon. As the stock market tumbled, a cottage industry of investment firms emerged urging IRA owners to direct IRA assets out of equities and into real property, real estate notes, and real estate investment trusts (REITs).<sup>2</sup>

No law prohibits an IRA owner from doing this, but many financial firms serving as IRA custodians do. So if you want to invest in real estate through your IRA, you must first check to see if your IRA custodian will allow it. If it is allowed and you proceed, you are on your own: your IRA will be self-directed, your IRA custodian will make no effort to advise you about your investment choices, and you alone will be responsible for your investment decisions. That is a risk you may or may not be willing to take.<sup>2</sup>

**Holding real estate in your IRA means looking at your IRA differently.** To lesser or greater degree, your IRA transforms from a dedicated retirement savings vehicle to a real estate investment vehicle. If you are more knowledgeable about the housing market than the stock market, you may prefer it this way.

Whether you know volumes about real estate or not, you must abide by the particular regulations and mechanics involved.

*Self-dealing is outlawed.* Legally, you can buy any form of real estate with your IRA assets, but you may not buy real property that will be used as your home or your place of business. Your IRA (which is by definition a trust) may not purchase any real estate that you own, or any real estate that is owned by a business in which you or certain members of your family have an ownership interest. It is also barred from selling any real property it holds to you or such business entities.<sup>1,2</sup>

*You buy or sell real estate through the IRA custodian.* The mechanics of making the actual transaction are fairly straightforward. You instruct your IRA custodian to authorize the purchase or sale of a property, providing the required documentation to facilitate that purchase or sale. The IRA custodian then commences to buy or sell the property for your IRA, with the title to the property vested in the name of the custodian. You have to have enough IRA assets to cover 100% of property management and property-specific expenses linked to the transaction; failing to have sufficient assets to cover those costs may mean penalties or forfeiting tax benefits.<sup>1</sup>

*Proceeds from sale & rental income go right back into the IRA.* This is necessary so that the account may retain its tax-deferred status. These newly invested assets get the same amount of creditor protection the IRA affords to other assets. The level of protection varies per state, though, and IRA assets are not protected against civil lawsuits.<sup>1,3</sup>

**Do you need to form an LLC?** Some owners of self-directed IRAs do just that, so that they can have checkbook control over their IRA assets. How does this work? The LLC sets up a bank account for the IRA owner, allowing him or her to write checks on behalf of the IRA. The LLC facilitates transactions for the IRA owner, instead of the IRA custodian.<sup>1</sup>

There are some notable benefits to adopting the LLC structure. Timing can be everything when it comes to a real estate transaction, and having a “checkbook IRA” gives you a chance to buy foreclosures on the steps of your local courthouse with IRA assets. An LLC structure may lower some custodial costs associated with IRA administration, and it also permits the IRA owner the option of handling some property management duties such as bill paying, advertising, and collection and deposit of rents. On the other hand, since an IRA is a trust from its inception, the LLC structure is technically superfluous.<sup>1,2</sup>

**If you want to hold real estate in an IRA, speak with a tax or legal professional first.** You must understand what you are getting into, and the full tax details are beyond the scope and length of this article. Using your IRA to invest in real estate could be an auspicious move; it could also breed complications. Remember that an IRA is not a prerequisite for real estate investment.

Sincerely,

*Phil*

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***If your plans for investment and retirement income that you believe to be true,  
turned out not to be true – when would you want to know?***

**Citations.**

- 1 - investopedia.com/articles/retirement/08/self-directed-real-estate-iras.asp?no\_header\_alt=true [1/11/16]
- 2 - money.usnews.com/money/blogs/the-smarter-mutual-fund-investor/2015/01/28/investors-see-benefit-in-using-iras-for-real-estate [1/28/15]
- 3 - chicagotribune.com/news/sns-wp-blm-retire-comment-ab936112-b3d0-11e5-8abc-d09392edc612-20160109-story.html [1/9/16]

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