Self-Directed Real Estate 101

How Does Real Estate Investing in a Retirement Account Work?

Part I: What Does it Mean to Self-Direct My Real Estate Investments?

Many investors are surprised to learn it is possible to invest in real estate using their retirement accounts.

Self-directed IRAs and other self-directed retirement accounts can hold a variety of assets, including real estate, tax liens, promissory notes, private entities, and more.

Many investors open self-directed accounts to diversify their portfolios with alternative investments, within a tax-advantaged environment.

Though some investors have never heard of the concept, self-directed investing is nothing new. Since IRAs were introduced in 1974, the IRS has only listed a handful of items that are not permitted in an IRA (the entire list can be found in *IRS Publication 590* at IRS.gov).

With a self-directed retirement plan custodian, any retirement plan can be self-directed.

There are several retirement plans available to investors; the most common are the Traditional IRA and the Roth IRA. These accounts are designed for individuals and offer tax-advantaged growth, but there are differences between them.

Traditional IRA	Roth IRA
• Funded with pre-tax dollars • If qualified, investors receive a tax deduction for the amount contributed in a given year • Tax-deferred investment growth while inside the account • Taxable distributions when withdrawn from the account • Subject to Required Minimum Distribution (RMD) requirements at age 72	• Funded with after-tax dollars (no tax deduction) • Tax-free investment growth while inside the account • Tax-free qualified distributions when withdrawn from the account • Subject to income eligibility requirements • Not subject to Required Minimum Distribution (RMD) requirements

For more details regarding income limits and contribution limits, visit www.IRS.gov.

Certain types of retirement accounts allow you to contribute more than $50,000

In addition to individual plans, business owners may have the option to take advantage of the Simplified Employee Pension (SEP) or Savings Incentive Match Plan for Employees (SIMPLE) IRAs. Both plans are designed for small businesses but may also benefit self-employed individuals.

The SEP and SIMPLE IRAs allow you to potentially make larger contributions than the Traditional and Roth IRAs. Both IRAs offer tax-deferred growth and yearly tax deductions. All distributions are subject to taxes.

Health plans can be self-directed, too...

A Health Savings Account (HSA) is a tax-advantaged account for individuals or their families with high-deductible health plans, allowing them to set aside funds for qualified medical expenses now and in the future.

Pay for your child's education as well...

The Coverdell Education Savings Account (CESA) is available to assist in paying for qualified education expenses. The plan can be self-directed in a tax-free environment and all distributions used for qualified education expenses are tax-free.

As you can see, there are a number of different types of self-directed accounts that allow you to invest in real estate (or other alternative assets). Depending on your specific situation and financial goals, it may be possible to take advantage of more than one of these plans.

It may also be possible to rollover or transfer an existing IRA, 401(k), 403(b), Thrift Savings Plan, or other retirement account to a self-directed custodian. Part II explains this process in more detail.

Part II: How Self-Directed Real Estate Investing Works

Here are the general steps to self-directed real estate investing:

1. **Open an Equity Trust Account**
   One of our specialized counselors will walk you through the process, or you can do it online with myEQUITY.

2. **Find an Investment Opportunity**
   A few potential sources:
   - Real Estate Listings
   - Other Investors
   - Acquaintances
   - Investment District online marketplace

3. **Decide How You Will Fund the Investment**
   Possibilities include:
   - Purchasing outright with your retirement account
   - Partnering account money with another source
   - Leveraging with non-recourse loan

4. **Direct Equity Trust to Fund Your Investment**
   Easily initiate your investment with the Real Estate Wizard in myEQUITY.

   Our liaisons are here to help you if you need it.

Part III: Self-Directed Investing Rules to Know

Investing in real estate in an IRA or other self-directed account requires that certain rules be followed to avoid incurring taxes or penalties. *IRS Publication 590* outlines these rules. Here are some guidelines to keep in mind.

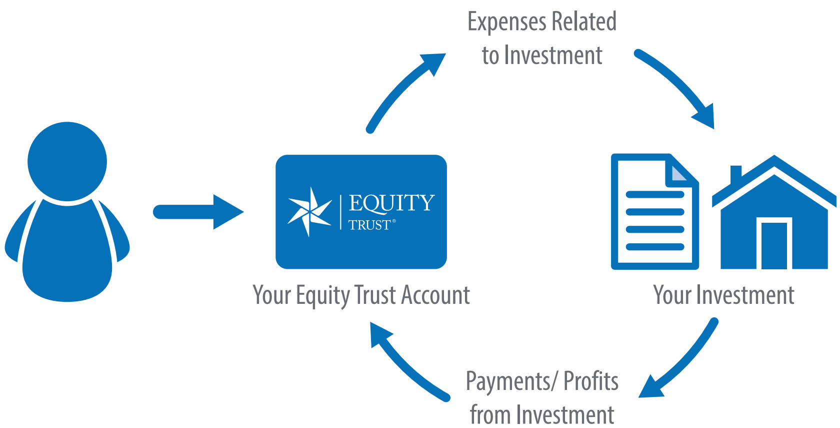
Investment must be at "arm's length"

IRS rules state that you and the investment must be at arm's length. In other words, you cannot directly benefit from an asset owned by your retirement account.

Your retirement account is designed to provide for your retirement and is not intended to benefit you now. You cannot receive a direct or indirect benefit from the property purchase. It's considered an "indirect benefit" if your IRA is engaged in transactions that, in some way, can benefit you personally.

A few examples include:

- **Using property held in the retirement account:** Using real estate purchased through your IRA as an office, personal residence, vacation home, retirement home, etc. is not allowed.
- **Receiving personal benefits from your retirement account:** You cannot lend yourself money from your IRA or pay yourself, or a company you own, to do work on a home purchased by your IRA.



Additionally, IRS rules state that a self-directed retirement account may not: buy an investment from, sell it to, or otherwise be involved with a "disqualified person." A disqualified person includes you as the account holder, service providers of the IRA, fiduciaries, family members of lineal ascent or descent, and entities of which 50 percent or more is owned directly or indirectly by a disqualified person.

Whenever making an investment decision, please consult with tax, legal, and accounting professionals.

Refer to the IRS for more information: Internal Revenue Code 4975 and *IRS Publication 590*.

Part IV: Frequently Asked Questions

I plan to purchase a rental property with my IRA. Does the rental income have to go back into my IRA?

Yes, all income generated by an IRA-owned property must return to your IRA. This ensures that you retain the tax-deferred or tax-free status of the investment.

When I sell a property owned by my IRA, may I keep a portion of the proceeds and send the remaining portion to Equity Trust?

No. All income generated from the sale of a property owned by your IRA must be deposited directly into your IRA.

Can I use funds from my IRA to renovate property to sell it at a higher price?

Yes. However, your IRA must pay all expenses associated with a property that it owns, including renovations. Further, all proceeds from the sale of the renovated property must be deposited into your IRA.

Can my IRA invest in a newly formed entity that will invest in real estate?

Yes. Investments in newly formed private entities, such as limited partnerships, limited liability companies, C corporations or land trusts, are permissible under the Internal Revenue Code, with the exception of subchapter S corporations.

How do I pay funds to the seller?

You must instruct your custodian where to send the funds from your account. Some custodians give you the option to do this online, or you can submit a form with the instructions. Typically, funding to purchase real estate is sent to a title company, attorney, or escrow agent.

Can my IRA purchase real estate that my corporation, partnership or LLC owns?

No. This is considered a prohibited transaction (see IRC 4975).

Can my IRA purchase real estate that I currently own?

No. This is considered a prohibited transaction (see IRC 4975). You may not purchase a property, or interest in a property, that's currently owned by a disqualified person, which includes yourself.

Am I restricted to only purchasing residential property with my IRA?

You are not limited to residential real estate. Your IRA can hold various investment properties such as commercial buildings, vacant land, condominiums, mobile homes and apartment buildings, in addition to residential property.

Contact Us.

For more information or to begin investing with an Equity Trust self-directed account, contact:

855-673-4721

www.TrustETC.com
help@TrustETC.com

The Equity Trust Advantage

You have your choice of self-directed IRA custodians. So why choose Equity Trust? The difference is clear.

- Nearly limitless investment options include stocks, bonds, mutual funds, real estate, private entities, cryptocurrency, and more
- State-of-the-art online account management system myEQUITY provides easy, around-the-clock account and investment management capabilities from any device
- More than 45 years as an industry-leading custodian specializing in alternative assets
- Clients from all 50 states have entrusted us to custody over $34 billion in retirement assets (as of 8/31/2021)
- Dedicated representatives provide personal service
- Regular educational and inspirational opportunities include newsletters, webinars, videos, case studies, in-person events, resource guides, and more

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