

Yes, you can use your IRA dollars to own international real estate.

By Larry C. Grossman

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Contrary to what you probably have been told by your broker or banker, you can own real estate in your IRA, including non-U.S. real estate. Over the years, advisors have wrongly convinced many people they cannot own real estate, as well as a number of other alternative investments, inside their IRA's or other retirement plans. Nothing could be further from the truth. In actuality, the IRS allows a great deal of flexibility when it comes to investing the assets of your retirement account.

The trouble comes if you don't have a "selfdirected" IRA or if you work with a custodian who imposes his own investment restrictions. Most of these restrictions have nothing to do with the code governing retirement accounts but are instead employed to make life easier for the custodian.

What's allowed—the real skinny

The truth is, the rules governing the ownership of real estate are simple...and you can own virtually any kind of real estate you could name in your IRA or other retirement account, including:

- Raw land
- Condos
- Office buildings
- Single-family homes
- Multi-family homes
- Apartment buildings
- Improved land

Prohibited transactions and self-dealing

The IRS has some simple and straightforward rules that define what you cannot do. A simple rule of thumb is your retirement plan is meant to benefit you at retirement and not before. You may not, therefore, directly or indirectly, deal with yourself or a disqualified person.

What does this mean? In short, that you cannot lend money, extend credit, or furnish goods, services, or facilities to yourself or a disqualified individual. In other words, you can invest in any type of real estate you want as long as it is an investment and not for your own use *currently*.

“Currently” is an important part of this puzzle. Let’s assume you have found your dream retirement home or the piece of property you would like to build it on. And, remember, as I’ve explained, the property can be in the United States or it can be anywhere else in the world that you’d like it to be. Someday, when you retire, you would like to own the property personally or have it for your own use. No problem. You can take possession of the property at that time, in effect taking it as a distribution of your plan.

You would be taxed on the value of the property at that time. Of course you could sell the property outright at anytime as well.

Other requirements:

- You may not purchase the property from yourself.
- You may not purchase the property from family members, with the exception of siblings.
- Neither you, your business, nor members of your family may lease or live in any investment property owned by your plan.
- Only retirement funds may be used as the down payment or good-faith deposit.
- The title must be in the name of the retirement account.
- Fractional ownerships are allowed.

Who is “disqualified”?

The relevant IRS code disallows you to deal with yourself or a “disqualified person.” Who is “disqualified”?

- 1) An owner, direct or indirect, of 50% or greater of:
 - The capital interest of a partnership.
 - The total value of all shares of stock of a corporation including all classes.
 - The combined voting power of all classes eligible to vote.
- 2) A member of the family, again with the exception of siblings.

These are the basic definitions of a disqualified individual, but there are other details related to this that you should understand depending on your personal circumstances.

Yes, there are special exemptions

One of the most exciting aspects to this idea of investing is that there are 10 government-approved blanket exemptions to the “prohibited transactions” as I have described them. Amazingly, these exemptions have been granted in areas that seemingly contradict the “self-dealing” provisions of the code.

In one exemption, a retirement plan was allowed to purchase the mortgage for the participants' primary residence with plan assets. In a second, plan assets were used to purchase the existing mortgage on a property currently being used for the participants' business. You, too, can make use of these blanket exemptions by following the government-approved process.

How to own

As you know, there are many ways to purchase real estate. You can own the real estate fully or you can own a fraction of it, with other entities or investors owning other fractions. You can purchase an option on the real estate or you can buy outright using a land trust, L.L.C., or similar entity.

All of these options are allowed for the kind of investment I'm describing. Furthermore, you can pay for the property in full using retirement assets or you can finance it. If the property is financed, you must take special care to structure the purchase correctly so as to avoid adverse tax consequences down the road.

The down payment must be paid for by the plan, and all future payments must come from the plan assets, new contributions, and/or income produced by the property.

If the property is fractionally owned by the plan, the down payment and an equivalent amount of the on-going payments must come from the plan. There are detailed instructions as to how to accomplish this from a custodian who allows these types of investments.

Taking on debt

If you wish to use your retirement plan to invest in real estate but do not have sufficient funds in your IRA, your IRA can incur debt. This debt/mortgage must be in the form of a non-recourse loan where the only recourse for default of the loan is the underlying real estate/property.

You can obtain your non-recourse loan from a lending institution, a private investor, or the seller of the property. (The loan, however, cannot originate from you or any family member of direct linear descent—for example, your grandfather/grandmother, father/mother, husband/wife, son/daughter, etc.) You cannot personally sign for the loan.

Managing the property

As a result of a recent tax ruling, some custodians will now allow you to act as your own property manager. You can collect a "reasonable fee" for this service from your retirement plan, and you will receive a 1099 at the end of the year for these fees.

Any income from the property must be returned to the retirement plan as a profit of the plan, less any expenses incurred. The plan assets can be used to pay administrative and record-keeping expenses as well. Conversely, you can hire an outside property manager to perform this service, provided they do not fall under the “disqualified person(s)” definition.

How do I do this?

The good news is you can find the property of your dreams anywhere in the world, purchase all or part of it with your retirement assets, and eventually take ownership of it—all completely legally. But, yes, you will need help to make sure you do not violate any relevant codes or take any missteps that will cause tax problems for you later on.

Fees for setting up the structure

It will cost you about \$100 to establish an account with a qualified custodian, including the first year’s annual fee. Thereafter, you’ll be charged an annual fee of \$100 to \$400 depending on the custodian and value of the account; a one-time fee of \$100 to review a real estate purchase; and a one-time fee of 1% of the value of the transaction (\$500 minimum).

For additional information, please contact me at:

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