

Real Estate Investing Using IRAs© 2006
by Tom Anderson

Did you know that retirement accounts can invest in real estate, including in many foreign countries? Did you know that there is \$3.7 trillion in IRAs in this country? And, did you know that there is an operation in San Francisco that has allowed IRA holders to invest in real estate for the past 16 years? Why should you care?

Well, let's take a closer look at your personal investment and retirement objectives. Maybe you're like many who have seen their retirement accounts decline significantly in value while they saw their taxable real estate holdings significantly increase in value over the past five years. Had you been aware of the option to invest your retirement account in real estate, in most cases, you could not only have avoided these retirement account losses, but you could have experienced extraordinary gains. On the other hand, you may just want to diversify your retirement portfolio to reduce the risk associated with tying all your assets up in one asset class (e.g., public stock). Or maybe you just want to have a little more control over your investing destiny, instead of entrusting your success to a CEO you'll never meet.

By understanding the opportunities through self-directed IRAs, you may be able to get your retirement planning back on track with your financial objectives. Besides real estate, the most important wealth building option for the majority of Americans comes from retirement accounts, including IRAs created by people who retire and roll their retirement accounts tax-free to IRAs. It has been established that many of the boomers now retiring and moving their 401(k)s to IRAs want to take more control over their destiny. Some, who are dismayed by all the securities, corporate, and accounting scandals, have consequently lost trust in their brokers. Others are simply unhappy with a volatile and unpredictable stock market. Finally, others are just very successful real estate investors who want to take advantage of their knowledge to enhance their retirement accounts, which can grow tax-deferred for many years.

Unfortunately, against this clear desire and demand from investors, most of the legally authorized firms providing IRA services restrict their clients' investment options to those investments in which there is an opportunity for them to be compensated. For example, a typical stock brokerage firm will only allow its clients to invest in the stock market while there are thousands of other possible and permitted investments including investment property of any kind.

Fortunately, there are emerging companies that are expanding Americans' opportunity to invest in what they know and thereby take control of their retirement. A self-directed IRA is different from a more traditional IRA in that the holder of the account must direct the investments. Self-directed IRA custodians can only act on the authorized instructions of their clients and can neither sell investments nor provide investment advice. While this fact can create a barrier to some, it is an opportunity for the more experienced real estate investor and/or their real estate broker, or anyone else who wants to take back control.

A self-directed IRA certainly is attractive to a baby-boomer approaching retirement. After having spent the better part of a career putting away tax-free money into a fund that either invests in the employer's stock, or a set of mutual funds, this individual is most likely looking forward to the freedom to controlling the destiny of their own retirement account. If you are a real estate investment knowledgeable investor, you should know that you can invest your retirement account in your real estate deals. If you believe, like many financial analysts that some of the best opportunities lie overseas, you'll be happy to know, that in most cases, you can invest your IRA there too! Take a San Francisco pediatrician who achieved a 281% return in two years investing in property in New Zealand through his IRA. He benefited not only from the local real estate appreciation at the time in New Zealand, but also an improvement in the exchange rate between the U.S. and New Zealand dollars.

Self-directed IRAs will enable millions of individuals to use the monies that have previously been tied up in traditional IRAs to invest in real estate. While real estate represents the largest component of the net worth (per capita) in this country (44%), it is estimated that only 2% is invested in through retirement accounts. That is primarily due to the fact that the major providers of IRA services do not promote the concept, because there is no reward to them for doing so. That's not really an acceptable reason for most investors who are more interested in improving their fortunes than those of their service providers. As more and more individuals learn about self-directed IRAs, there will be a shift of a significant amount of retirement assets into real estate and private equity both here and abroad.

It gets even better, too. It is now possible for an IRA to get up to 70 percent bank non-recourse financing to purchase income-producing investment properties anywhere in the U.S. The fact that an investor can experience similar benefits that can be experienced through leverage with taxable investments dramatically increases the investment yield for their IRA. In fact, this new feature (only 2 years old) can result in tripled or greater returns when a mortgage is added to the funds from a self-directed IRA. When an IRA invests using leverage, there is a tax of income and capital gains associated with the amount leveraged (in most cases), so be sure to have a knowledgeable CPA to help you at year-end. Nevertheless, the effect of leverage, even after tax, can quadruple the results of an all-cash IRA real estate investment. Once the word gets out to the average American (and it will), there will be even more interest in the self-directed investing area that is already growing at 25%.

Possible real estate investments permitted within IRAs include ocean front property in Costa Rica, a condo in Lithuania, a commercial building in Shanghai, a residential rental in Arkansas, a boat slip on Lake Erie, or even a parking lot in Dallas. Virtually any type of property can be purchased as long as it is strictly for investment purposes, which means that you and your direct relatives cannot make use of it personally. But, if you are simply looking to use the purchase of real estate as a means to grow your retirement account and to hedge your portfolio from potential losses, which could be associated with tying up all your assets in a single asset class (e.g., stocks), all you have to do is get started.