FINANCIAL ADVISORY

Partial Interest Holdings as 1031 Exchange Replacement Properties

BY CHRISTOPHER MILLER, MBA
SPECIALIZED WEALTH MANAGEMENT

For seventeen years now, I have helped investors complete fully tax-deferred 1031 Exchanges by buying partial-interest replacement properties. This month, I will talk about what that means and how these properties work. Then we'll see if they may be right for you.

WHAT ARE PARTIAL INTEREST PROPERTIES?

I work with real estate syndication companies, (I also call them "program sponsors"), that buy large investment properties and resell them to investors. After these sponsors re-sell a property to investors, they will then stay on as the property and asset manager. This part is important to me – I want to see the sponsor stay on as a manager to guide the property through the business plan they've set up for it. Through my years in the business, I have watched how these companies manage their buildings and how they perform for investors. Today, I choose to work with only the companies that I feel are the best. These firms that I work with are all focused on partial interest properties for the majority of their business – I would rather avoid a company that does this "part-time."

These sponsors will send me their latest deals when they are available. I will then start my due diligence review by drawing on my real estate finance and acquisitions experience. If I like what I see, I will share that property with my investors. I don't always like what I see – even from companies that I work with a lot. This isn't a knock on those companies – I feel that I owe my success in this business to being more selective about the deals that I recommend.

THESE PROPERTIES CAN BENEFIT MANY GROUPS OF INVESTORS

Many of my clients are older and would like to retire from landlording, but have children that are unable or uninterested in taking over "the family business." Some may be busy with young children and a career of their own, while some may live out of state. These investors have worked hard for a lifetime to build up substantial equity in their investment properties and, understandably, are not thrilled at the prospect of paying a large chunk of their savings to the government in taxes. They also know that, upon their death, all of their capital gains and accumulated depreciation taxes will disappear – and the property will then pass to their heirs tax-free. (Estate taxes are a possibility – but that is a subject for another article.) So – are they stuck with a life sentence as a landlord?

Please turn to page 24

Christopher Miller is a Managing Director with Specialized Wealth Management and specializes in tax-advantaged investments including 1031 replacement properties. Chris' real estate experience includes work in commercial appraisal, in institutional acquisitions for a national real estate syndicator and as an advisor helping clients through over three hundred 1031 Exchanges. Chris has been featured as an expert in several industry publications and on television and earned an undergraduate business degree and an MBA emphasizing Real Estate Finance from the University of Southern California. Chris began his real estate career in 1998, began working in the partial interest industry in 2001 and has been a broker advising clients since 2003. Call him toll-free at (877) 313 – 1868.

Continued from page 22

Thankfully, the answer is "no" – partial interest properties can offer them a way out. By exchanging into such a property, my clients can defer those taxes, (perhaps forever), and preserve the income and growth potential from the full amount of their built-up equity. Upon their death, their children will inherit this income and growth potential and can then "cash out" when the property sells at the end of its' business plan.

INVESTORS WHO WANT TO GET THEIR MONEY OUT OF CALIFORNIA

Some of my investors are additionally motivated by a desire to move their real estate money out of California. With property values at high points once again, they feel that growth in California may be slowing over the next decade or two. As anyone who regularly drives our freeways has seen, we're running out of places to put everybody. These clients feel that now may be a great time to sell at "the top" in California and invest somewhere that has the potential to be "the next Orange County" in 20 years. Certain areas in Texas, Georgia and Florida look promising, but managing a property that is at least 3 hours away by airplane does not. Exchanging into a partial interest property and leaving the management to a professional company can be an attractive alternative.

INVESTORS WHO NEED A REPLACEMENT PROPERTY NOW!

Over the years, I have helped many a client avoid an unpleasant tax bill when their "Plan A" 1031 Exchange fell through. For the 1031 Exchange, the IRS has given us a very firm timeline to follow – identify some properties that you might buy within 45 days and close on one, some or all of them in 180 days. Often, an investor is nearing his 45th day when he discovers that his preferred property is "junk." Is he then stuck paying the taxes if he doesn't quickly commit to another property – and just hope that due diligence runs smoothly on that one?

With partial interest properties; the answer is, again, "thankfully – no." These partial interest properties are "turn-key": ready to close. Due diligence has been done and a loan (if applicable) has been arranged. This means no loan application and approval process for the investors. No inspections to schedule. We could fill out paperwork today, have you closed by next week and get you your first income check next month. This could be a much better option than starting due diligence on yet another property.

This article is necessarily a short summary of my work in partial interest replacement properties for 1031 Exchanges. My past articles contain more information on how I analyze potential properties, what sort of asset classes work best, and what geographic locations I prefer. Of course, if you would like to learn more, call my office toll-free at (877) 313-1868.