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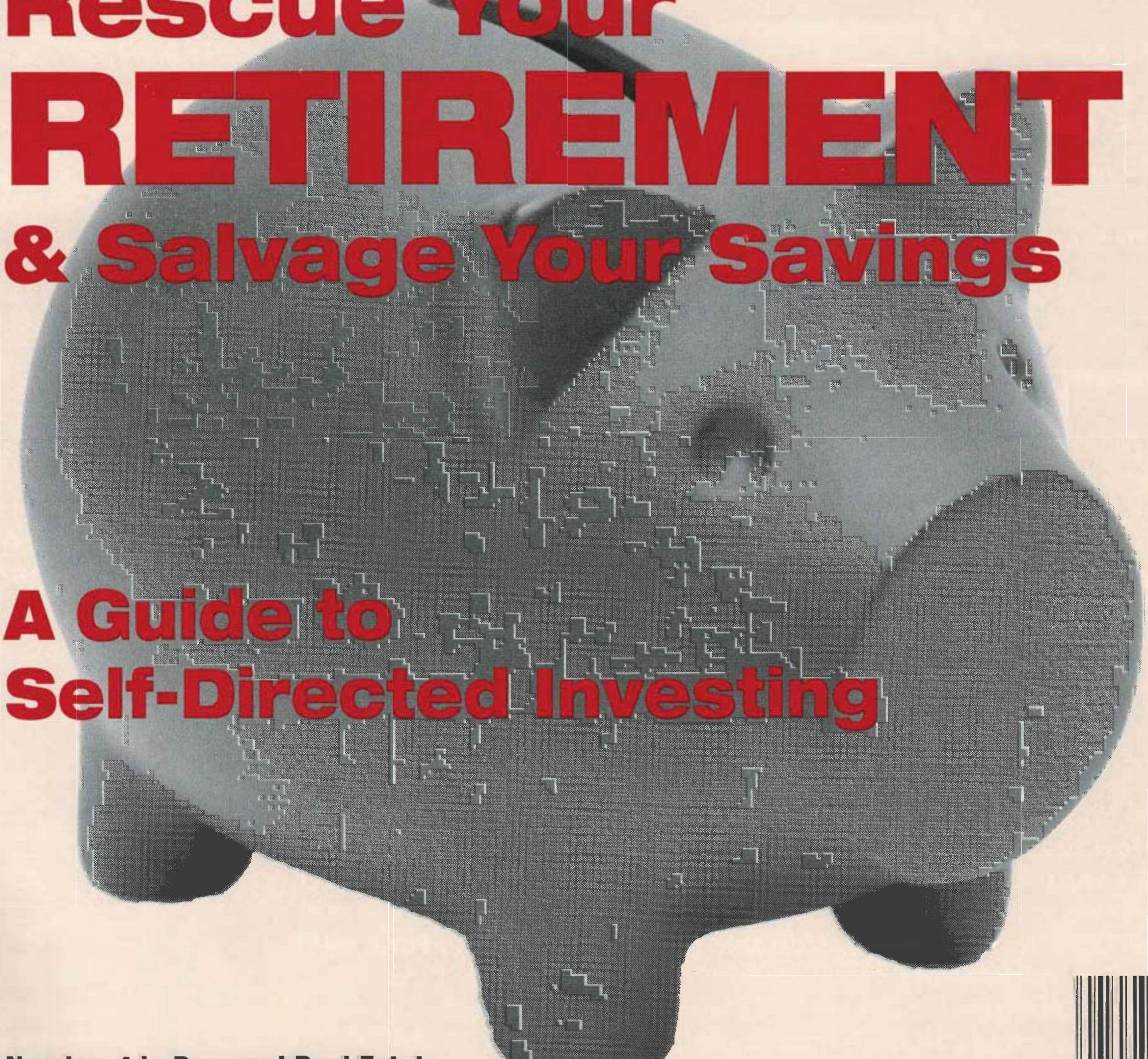
Investor Review

Rescue Your RETIREMENT & Salvage Your Savings



A Guide to Self-Directed Investing

Number 4 in Personal Real Estate Investor Magazine's Investor Review Series

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ANSWERS TO CLIENTS' FREQUENT QUESTIONS

By Dmitriy Fomichenko
Sense Financial

Q. I have been hearing about self-directed IRAs lately and would like to know what the qualifications are to establish one.

A. As far as the IRS is concerned, a self-directed IRA is no different than a conventional IRA. A self-directed IRA has the same contribution and distribution rules. The same rules for required minimum distributions are applied to both.

The only difference between the two is that with a conventional IRA your custodian limits your investment choices, while with a self-directed IRA your choices are virtually limitless.

So the short answer is: Anyone who has earned income or has another retirement account eligible to be rolled over or transferred can open self-directed IRA. There is no minimum amount.

Q. My wife and I both have small IRAs, which individually not big enough to invest. Can we combine them into one self-directed IRA to invest?

A. IRA stands for Individual Retirement Account; therefore, it is set up in one individual name. You cannot have two names on one account. So you cannot combine a husband and wife's IRA into one. However, there are ways to pull the funds from spouses' IRAs together and invest jointly. This can be done by having two self-directed IRA account partners on a deal or setting up a checkbook IRA (IRA-owned LLC) with two partners.

Q. I am self-employed. Should I choose a self-directed SEP (simplified employee pension) IRA or Solo 401(k)?

A. As a self-employed individual, you qualify for both. However, when you carefully consider the options and benefits that each of these accounts offers, the answer is obvious: Solo 401(k) is a winner.

Q. Can I transfer property that I already own into my IRA?

A. No. You are considered to be a disqualified person for your IRA; therefore, transacting any business between you and the IRA is strictly prohibited under Internal Revenue Code Section 4975. You need to avoid "self-dealing" and instead look for another investment opportunity for your IRA.

Q. I only have enough in my IRA to finance a down payment. Can I take out a loan for the rest?

A. Yes, but it has to be a non-recourse loan. This is a type of loan in which the lender only has recourse to the specified asset, but not to the borrower himself. You can access this kind of loan through a company that specializes in non-recourse lending. (Your self-directed IRA provider should be able to provide you with a list of such companies.)

Q. Do I have to do a rollover to finance a self-directed IRA?

A. No. You can start a self-directed IRA with just an initial contribution.

Q. If I do a rollover from a standard IRA into a self-directed real estate IRA, will the IRS penalize me?

A. No. A self-directed IRA is the same as any other retirement plan. As long as the IRS is notified within 60 days of the rollover, there are no taxes or penalties.

Q. Are prohibited transactions more of a concern with a real estate investment?

A. Good question. Before we answer that, though, let's first define what we mean by a prohibited transaction. The government has mandated that the investor (and his or her close linear relatives) may not give or receive any benefit from the retirement investments.

Giving benefit includes personally doing maintenance on a property, personally paying a property's bills or letting your son act as paid worker for the property.

Taking benefit includes using the property as a vacation home, renting it out to your children or using it as collateral in an unrelated dealing. The general name for this type of infraction is prohibited transaction.

Now, let's get back to the question. If you plan on mowing the lawn, doing the painting and taking care of other property-related work yourself, then the answer is yes; those would all be considered prohibited transactions. However, if you purchase the property and then use contractors and other workers to run the property, then that is allowed. Additionally, the investor himself may also do any paperwork or managerial duties for the property.

An easy way to think about it is that physical labor is prohibited, while desk labor is permitted. Before you do anything, pose the question to your self-directed provider or real estate attorney. Better safe than sorry.

www.SenseFinancial.com
949-228-9393

ABOUT THE AUTHORS

Dmitriy Fomichenko is the President of Sense Financial, a company specializing in helping clients obtain checkbook control over their retirement accounts. Since 2000, he has been helping his clients maximize returns on their investments, while protecting their hard-earned money. He is passionate about helping families and individuals achieve financial freedom by following proven Biblical principles of prudent planning and investing.