How to Partner With Your Own Self-Directed IRA

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Partnering with your own Self-Directed IRA is just one strategy that I've seen more and more investors implement to try to help boost their retirement savings. Simply put, this strategy combines personal money with your retirement plan's money.

This tactic may allow you to expand your investment opportunities, because your pool of capital is larger from combining your available funds, earn a potential profit that is not currently taxed and take advantage of an opportunity to convert your Traditional IRA to a Roth IRA.

However, the "catch" of this strategy is that structuring your investment becomes crucial, and therefore, there are a few things you should be aware of before diving in. The following are three main elements to consider when partnering with your Self-Directed IRA.

1. **Acquisitions**
    - All entities must be named on all paperwork.
        - Remember, you and your IRA are two separate legal entities, which is why this type of partnership is possible. Although you are technically still considered to be a "disqualified person," this type of arrangement is possible because you are not buying, selling, lending or borrowing to or from your IRA or using your invested property as a personal resource.

    - Each entity owns an undivided interest of the property, which is sometimes referred to as tenants in common. This means that each entity controls only its percentage of the property and nothing more. This type of ownership also allows your entire percentage of the property to be inherited by a designated beneficiary or heir upon your passing.

    - The percentage of ownership is determined by the total initial dollars invested in the property. For example, if you are partnering with your IRA to invest in a property with cash, that costs $100,000, and you personally invest $20,000, then you personally own 20% of the property because you paid 20% of the initial cost. That requires your IRA to pay the remaining $80,000, giving your IRA 80% ownership because it paid 80% of the initial cost. After making the initial investments, you are never able to shift income by assigning a smaller or larger ownership to your IRA.

2. Maintenance

- Because income and expenses are pro-rata, each deposit and payment must be received or paid by each entity based on the percentage of ownership.

    - An example of this is if your property is billed $1,000. Since you own 20% of the property and your IRA owns 80%, you are required to personally pay $200 (20%) of that bill and your IRA is required to pay the remaining $800 (80%). The same conditions apply to money earned, such as tenants' monthly rent.

    - It's also important to note that the two entities CANNOT alternate between paying reoccurring bills, such as electricity or water, and that each entity must pay every bill in proportion to its share in the property.

  - The easiest way to accommodate this constraint is by hiring a third entity, such as a property manager, and explaining the required procedures for this type of investment to him/her. This person would then receive all income and pay all bills associated with the property and then either distribute or obtain the funds accordingly to/from each of the two entities.

3. Sale

- The property is also sold pro-rata, so each entity's income is directly proportional to the percentage of ownership. To continue with the prior example, if that same property sells for $150,000, you would personally receive $30,000 (20%), and your IRA would receive $120,000 (80%).

  - It is also permitted that only one entity sells its share if you would prefer that the other entity continue ownership, as long as that share is not then purchased by the other original entity. That transaction would not be permitted under the disqualified persons rule.

  - Any income deposited into your IRA account is tax-deferred in a Traditional IRA and tax-free in a Roth IRA. Income deposited to your personal account is subject to whichever tax benefits are available for your specific type of invested real estate.

As the owner or potential owner of a Self-Directed IRA, it is your responsibility to determine whether an investment is right for you and your individual portfolio. As with any financial transaction, it may be worth consulting your team of financial advisers before finalizing any deals.

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