A Real Estate Investor's Solution in a "Seller's" Market
By Jeff Cederberg

Today, on the Central Coast, we find ourselves in a real estate market that has seen an incredible rise in the prices of real estate properties over the past 3 years. As residential home owners we are very happy about this rise, but what if we own investment property and want to capture some of that appreciation?

The best time to sell has always been in a "seller's" market, so to capture that appreciation many investors will sell their properties. But, because of IRS rules on capital gains, if those properties are not replaced with "like kind" properties, most investors will face a large tax bill. To avoid that tax bill, most investors will replace their properties with something that is equal or greater in value. The problem then is that the investors become "buyers" in order to replace that property. Buying investment property in a "seller's" market is not the best investment strategy.

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The solution to this problem is simple. We want to sell in a "seller's" market with high prices and find replacement properties in "buyer's" markets with low prices. But how is that possible?

Finding the "buyer's" markets can be a difficult task even for the most seasoned real estate investor. This task is made more difficult because we must explore markets that are sometimes many miles away and we just don't have the time to spend researching properties in unfamiliar markets. Taking into consideration the time constraints of a 1031 Exchange with its 45 day replacement property identification rule, the race to find suitable replacement property and perform due diligence on those properties seems impossible. All of that research takes time and is often not possible in just 45 days.

There is a new option for investors to own investment real estate properties that has emerged in the last 8 years. It is called Tenant in Common or 'TIC' Property. These properties are usually triple net leased and/or have professional management in place. TIC properties are large institutional Commercial properties in all asset classes and multi family apartments with market values of $10,000,000 to over $150,000,000 with investment amounts starting from $150,000 to over $2,000,000. They are usually found in "buyer's" markets nationwide. The properties have a non-recourse loan (no personal liability to the investor) already in place. TIC properties have 3 or more levels of due diligence completed which usually exceeds that which is done on typical real estate transactions. TIC properties usually have a first year cash on cash flow of 7-8 % - add to that appreciation and the depreciation schedule and you're able to shelter 50% or more of your cash flow depending on the property chosen.

Now you're saying to yourself, "this sounds great but my property is doing well right now and I am getting good cash flow, so why should I deal with selling my property and dealing with all the hassle of finding something new?"

To answer that question, let's take a look at two different hypothetical real estate investors who own property on the central coast. Each has two similar rental homes that were bought five years ago for $250,000 each. These homes are currently worth about $530,000 each. The four rental homes are generating $1,200 a month in income each, for a total of $2,400 a month for each investor. Both of the investors manage the properties themselves to keep their costs down. In the current market, the rents that the investors are able to charge do not match the current real estate prices, so they are considering selling their properties to capture some of the appreciation that is not reflected in the rents they are able to charge.

The first investor has decided to sell his properties. He plans to do a 1031 Exchange to defer his capital gains taxes and buy Tenant in Common investment property. So he lists his two properties with a local Realtor and waits for them to sell. Upon selling, the first investor uses a 1031 Exchange and defers his capital gains taxes, depreciation recapture and 3 1/3 % taxes on sales price. He now has $1,000,000 in cash to invest after closing costs in Tenant in Common properties. In order to diversify, he decides to split the cash into two different asset classes in two different markets. He buys and now owns title to a 10 story office building in Las Vegas and a 400 unit apartment building in Phoenix as a Tenant in Common fractional owner. The properties he has chosen have first year cash on cash flow of 7 % with .5 % projected increase per year which should grow to 9 % in the fifth year with no property management.

The second investor decides to stay with his investment properties on the central coast.

Let's take a look at the performance over the NEXT five years for each investor's property portfolio.

Annual Cash Flow	Investor 1	Investor 2	Annual Variation Between Investors
Year 1	$70,000	$28,800	$41,200
Year 2	$75,000	$31,200	$43,800
Year 3	$80,000	$33,600	$46,400
Year 4	$85,000	$36,000	$49,000
Year 5	$90,000	$38,400	$51,600

In this scenario, Investor 1 has more time to spend with family and friends because he/she doesn't have to manage his properties and the income from his properties is much higher than the second investor who not only has lower income off his investments, but also must deal with the day to day management of his properties.

At the end of 5 years the first investor will sell their Tenant in Common properties usually in a "seller's" market and then reinvest their proceeds in another Tenant in Common property in a "buyer's" market and continue their acquisition of wealth. At the end of five years the second investor will be in the same situation he was in five years ago – hoping to sell in a "seller's" market but being forced to buy in that same "seller's" market.

Tenant in Common or 'TIC' properties provide Real Estate Investors with a solution to selling their properties in a "seller's" market, capturing the appreciation they have experienced over recent years, increasing their monthly cash flow and allowing them to continue to grow their wealth while spending less time managing their real estate investments.

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