GRACE CAPITAL MANAGEMENT

DELAWARE STATUTORY TRUSTS
DST INVESTING

SELLING REAL ESTATE, AND LOOKING TO DEFER CAPITAL GAINS TAXES?

Master the 1031 Exchange & Explore Alternatives to Buying Replacement Property

Tax Deferment • Passive Income
Liability Removal • Estate-Planning
Investment Return

1031WITHGRACEDST.COM

STORY: THE TYPICAL DST INVESTOR

The Typical DST Investor: Embrace Freedom to Enjoy What Matters

The Cohen couple, now in their golden years, want to enjoy retirement and to be more a part of the active lives of their grandchildren by reducing obligations. Having accumulated a portfolio of real estate over the years, they enjoyed the financial benefits but have grown tired of the “terrible Ts”: Tenants, Taxes, and Toilets. They have wanted to offload these assets, but have remained frozen with concern over the capital gains taxes involved.

Thankfully, they have a savvy financial advisor, who suggests the strategic solution of Delaware Statutory Trust (DST) investments. DSTs, compatible with 1031 Exchange rules, offer a way to reinvest the full amount of any capital gains into diversified, income-producing securities, freeing them from their real estate burdens.

So, the Cohens decided to sell, transitioning from hands-on property management to receiving passive income from DSTs, trusts with professionally managed, institutional-grade real estate. This shift gave them higher asset quality with the potential for appreciation and streamlined their estate planning. Their heirs receive a step-up in basis, eliminating deferred taxes and simplifying wealth transfer. DSTs foster peace where sometimes there are family squabbles and feuds over property.

The move to DST investments was a significant improvement in their quality of life. The Cohens preferred this method of deferring taxes while potentially generating passive income and returns, versus the burdens they had been under with direct property ownership.

INTRODUCTION TO 1031 EXCHANGES

Unlock the Power of Tax Deferral with a 1031 Exchange

What is a 1031 Exchange?

A 1031 Exchange allows investors to defer capital gains taxes on the sale of an investment property by reinvesting the proceeds into another "like-kind" property. (It is named after Section 1031 of the U.S. Internal Revenue Code). This tax-deferral mechanism can alternately be utilized by investing in Delaware Statutory Trusts (DSTs), where investors acquire shares in a Trust that owns institutional, professionally-managed property. This offers a flexible and diversified approach to real estate investment while operating within the 1031 Exchange framework.

Why is the 1031 Exchange a real estate investor's BFF (Best Financial Friend)?

Tax Deferral: Keep your hard-earned money working for you by deferring capital gains taxes and reinvesting 100% of your sale proceeds into a new property or DSTs.

Portfolio Diversification: Expand your real estate holdings by exchanging one property for multiple properties, or vice versa, to spread your risk across different types of investments in diverse market areas.

Estate Planning: Pass on your real estate investments to your heirs with a "step-up in basis" to the property's current market value at that point, effectively eliminating their capital gains tax liability.

Leverage: Use the equity in your current property to acquire a higher-value replacement property or DST, increasing your cash flow and potential appreciation over time.

Management Efficiency: Exchange a high-maintenance property for a lower-maintenance one, freeing up your time and resources for more lucrative investments.

Long-term Wealth Building: Repeatedly use 1031 Exchanges to defer your capital gains tax and reinvest the proceeds into more productive properties, building significant long-term wealth.

UNDERSTANDING 1031 EXCHANGES

The Essentials of 1031 Exchanges: A Path to Tax Deferral

1 PLAN AHEAD

BEFORE selling your property, consult with a 1031 Exchange specialist to ensure eligibility and make a plan.

2 SELL YOUR PROPERTY

Complete your sale. The proceeds **MUST** be transferred to a Qualified Intermediary (QI), instead of you directly, to defer taxes.

3 IDENTIFY REPLACEMENT PROPERTY

Within 45 days after selling your property, formally identify potential replacement properties. You can select up to three properties of any value, following the "Three Property Rule," or more under certain conditions.

4 PURCHASE REPLACEMENT PROPERTY

Within 180 days of the original sale, close on one or more of the identified properties. The replacement purchase(s) must be of equal or greater value to fully defer capital gains taxes.

5 MATCH OR EXCEED DEBT LOAD

The debt on the replacement property(s) should match or exceed the debt on your sold property to maximize tax deferral.

6 COMPLETE THE EXCHANGE

The QI will use the proceeds they are holding from the sale to purchase the replacement property on your behalf, completing the exchange.

7 REPORT TO IRS

File Form 8824 with the IRS during tax season to document the 1031 Exchange and the deferral of capital gains tax.

Remember, timing is critical in a 1031 Exchange, and each step must be carefully executed to ensure tax deferral.

THE LIMITATIONS OF THE REAL ESTATE OPTION

Direct Real Estate Investment: Navigating the Challenges

Navigating the intricacies of a 1031 Exchange can be challenging, and there are potential pitfalls that you should be aware of.

Identifying Replacement Property:
One of the biggest challenges is identifying a suitable replacement property within the short, 45-day identification period. An experienced real estate professional is a necessity.

Securing Financing:
You have a total of 180 days to lock down financing, so it's a good idea to start working with a lender early in the process. Taking on more debt for the replacement property can help you defer more capital gains taxes, but it also increases your financial liability and risk.

Maintaining Equal or Greater Leverage:
To fully defer capital gains taxes, the net market value and leverage on the property acquired must be the same as, or greater than, the property sold. This can be challenging. A qualified intermediary (QI) will calculate the necessary leverage and ensure that the 1031 exchange is structured correctly. DSTs can balance this equation.

Avoiding Constructive Receipt of Funds:
This means that you cannot have direct access to the sale proceeds at any point during the exchange process. The QI should hold the funds in escrow until they are used to purchase the replacement property. Make sure to choose a reputable QI with appropriate bonding.

Structuring the Exchange Correctly:
The 1031 Exchange process must be established and in place at or before the closing of the first property in the exchange. This means that the QI must be selected and the exchange agreement must be in place before any transactions occur.

Conclusion:
As powerful a wealth-building tool as the 1031 Exchange can be, navigating the complexities and timing of the real estate replacement process is challenging.

INTRODUCTION TO DSTS

Delaware Statutory Trusts (DSTs): Revolutionizing Real Estate Investments

Why a Delaware Statutory Trust?

1. Move from active property management to passive income as well as streamlining estate planning
2. Protect the 1031 Exchange with backup options, and reinvest the "boot" (leftover funds not used in the Exchange, subject to capital gains taxes)

Key DST Considerations:

Income Distribution: Regular monthly income distributions provide a steady cash flow to investors.

End of Life Cycle: At the end of the DST's term, the property is sold, potentially resulting in profit distribution to investors. The typical life cycle is 5-7 years.

DSTs are securities: shares in a real estate-related investment, available ONLY to "accredited investors".

Tax-deferment: DSTs follow the 1031 Exchange rules to qualify.

Professional Control: Management decisions rest with the Trust Sponsor, not individual investors.

No Ongoing Costs: No ongoing expenses, as is common when you manage real estate directly.

No Liability: Limited to the amount invested, with no responsibility for property debt or property liabilities.

Shielded Ownership: You hold a beneficial interest in the DST, not direct property ownership.

ADVANTAGES OF DSTS

The 3 "paydays" of a DST

1ST Tax-deferment results in immediate tax savings and reinvestment of 100% of your capital gains.

2ND Potential regular monthly income from DST profit distributions. May be tax-exempt!

3RD The return of your principal + profit from the sale of the DST property.

EXAMPLE OF A FUNDED DST

Engagement: Traditional Real Estate vs. DSTs in a 1031 Exchange

	TRADITIONAL REAL ESTATE INVESTMENT	DST INVESTMENT
Personal Engagement:	1. Active Management: Directly involved in such tasks as tenant screening, lease management, and regular property maintenance.	1. Passive
	2. Decision Making: You frequently make decisions regarding property upgrades, tenant issues, and finances.	2. None
	3. Problem Resolution: You handle emergencies and unexpected issues such as repairs or tenant disputes.	3. None
	4. Time Commitment: You invest significant time, especially if managing multiple properties or dealing with highmaintenance units.	4. None
Financial Engagement:	1. Initial Capital Outlay: You are typically required to invest a substantial amount up front for down payments, closing costs, and potential renovations.	1. Fixed Initial Investment
	2. Ongoing Costs: Your increasing expenses include annually rising property taxes and insurance, and possibly high maintenance and management fees.	2. No Extra Costs
	3. Variable Income: Your rental income can be unstable, influenced by market conditions, vacancy rates, and tenant reliability.	3. More Stabilized Income
	4. Resale Considerations: You have the potential for good returns upon a sale, but this is subject to market conditions, timing, and closing costs.	4. Targeted Exit Strategy

CONCLUSION:

The choice between traditional real estate and a DST in a 1031 exchange largely depends on your desired level of personal involvement and risk tolerance. Traditional real estate gives you more control and potentially higher returns but requires ongoing personal and financial engagement. In contrast, DSTs offer you a passive investment option with targeted returns and NO personal involvement, **making them ideal for you if you are looking to simplify your life.**

Unlock the Power of Tax Deferral with a 1031 Exchange

Here's the story:

When Academy Sports & Outdoors was gearing up to go public, their brand new headquarters in Katy, TX, was clearly a financial burden due to its high tax liabilities. The creative resolution? They sold the huge facilities to a DST sponsor while securing a leaseback agreement. This pivotal strategy converted a major taxable asset into a deductible office expense, refining the company's financials and boosting its attractiveness to the stock market. For DST investors, this maneuver created a dependable and lucrative income source throughout the life of the trust, a great illustration of the stability and profitability of investing in DSTs.

Facts:

210,300 square feet of corporate office space in West Houston.

Maximize rental revenue and distribute annual cash flows.

Anticipated Debt: $35,500,000
Equity from investors: $27,475,000
Anticipated Leverage: 56.4%
Amortization: 10 Years Interest Only
Estimated Distribution for Years 1-5: 6.0%; Years 6-10: 6.61%

WHICH IS RIGHT FOR YOU? PROPERTY VS. DST

Real Estate: The Tried and True Investment

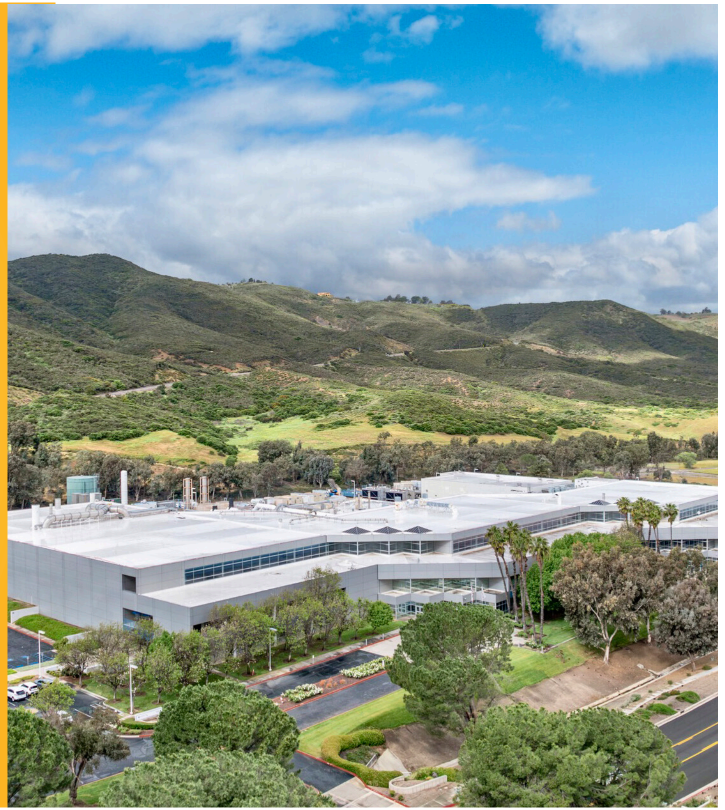
DIRECT OWNERSHIP:
You have complete control over your property, from management decisions to renovations.

DIVERSE OPTIONS:
Choose from a wide range of property types, including residential, commercial, and industrial.

POTENTIAL FOR APPRECIATION:
Real estate can increase in value over time, leading to significant gains.

CASH FLOW:
Rental properties can provide a steady stream of income.

INHERITANCE:
Pass properties to your heirs, with a step-up in basis.



DST Investments: The Modern Approach to Real Estate

FRACTIONAL OWNERSHIP:
You can buy shares in trusts that own high-quality, institutional-grade properties.

ELIMINATE THE MANAGEMENT BURDEN:
The DST Sponsor handles management and the day-to-day operations, so you can sit back and relax.

DIVERSIFICATION:
You can invest in multiple DSTs; residential, commercial, or industrial in different markets, reducing risk.

RETURNS
Potential monthly cash flow, as well as the potential for your share in the profits when the property is sold.

ESTATE PLANNING:
Simplify inheritance, passing down shares with a step-up in basis, eliminating capital gains taxes deferred up to that point.

WHAT IS MEANT BY "LIKE-KIND" PROPERTY?

In a 1031 Exchange, "like-kind" does NOT mean replacing a rental duplex with another duplex in the same city, in other words, similar real estate... this confuses people! Rather, it is legal language that refers to the nature or character of the property rather than its grade or quality. Take a look at this list, illustrating the variety of exchanges, considered "like-kind" for your property:

1. **Commercial Office Buildings**
2. **Retail Properties:** Includes shopping centers, retail strip malls, or standalone stores.
3. **Industrial Facilities:** Warehouses, distribution centers, or manufacturing plants.
4. **Residential Rental Properties:** Apartment buildings, duplexes, or any other property rented out to tenants.
5. **Raw Land**
6. **Agricultural Land:** Farms, vineyards, or ranches
7. **Special-Purpose Properties:** Like-kind exchanges can also include properties like hotels, hospitals, parking lots, storage units, and more.
8. **Mineral Rights and Water Rights:** Yes, even these can be exchanged, provided they are held for investment purposes.
9. **Delaware Statutory Trusts (DSTs):** Investors can exchange real estate for an interest in a DST, allowing for investment in larger, potentially institutional-quality properties.

DST INVESTMENTS IN 1031 EXCHANGES: QUICK FAQS

1. What is a DST?

A Delaware Statutory Trust (DST) is a vehicle for fractional ownership in a trust, which owns institutional-grade real estate and is eligible for 1031 tax-deferred exchanges.

2. How does a DST fit into a 1031 Exchange?

The DST was specifically created to conform to the 1031 Exchange rules, to be a security alternative to reinvesting in real estate, while defering capital gains taxes.

3. What are the minimum investment requirements?

Most DSTs require a minimum investment of $100,000 in 1031 Exchanges. Above that, you can buy fractional shares to meet any amount.

4. Benefits of DST investment?

Access to premium real estate, professional management, portfolio diversification, and the potential for steady income, along with the opportunity to share in profits when the Trust property is sold.

4. Who can invest in a DST?

Accredited Investors, defined by income of $200k/year ($300k for couples) or a net worth over $1 million, excluding the primary residence.

5. Is a DST good for estate planning?

Yes, it allows for inheritance with potential tax advantages like a step-up in basis.

6. What are DST risks?

Risks include property depreciation, market fluctuations, and potential foreclosure, just as in owning real estate directly.

7. DST investment duration?

Usually 5-7 years, based on the trust's strategy and real estate performance.

8. Can I sell my DST share early?

DST shares are illiquid, with limited options for early sale, typically relying on secondary markets or special redemption programs.

BEGIN YOUR DST INVESTMENT JOURNEY TODAY

Earl Proeger

DST@GRACE-CAP.COM | 512-293-7731

11651 JOLLYVILLE RD, #300 AUSTIN, TX 78759

GRACE CAPITAL MANAGEMENT

1031WITHGRACEDST.COM