NON-RECOURSE LOANS FOR REAL ESTATE INVESTING:

HOW TO GET A LOAN FOR YOUR SELF-DIRECTED IRA

IRAR TRUST COMPANY

IRA RESOURCES, INC.

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Introduction

If you've ever considered real estate for your retirement portfolio but felt limited by your IRA's size, combining a self-directed IRA with a non-recourse loan can be a powerful solution.

What Is a Non-Recourse Loan?

Non-recourse loans are a unique type of financing popular for real estate investments in IRAs. Unlike traditional loans where the borrower's personal assets are on the line (e.g., house, car, savings), a non-recourse loan offers limited liability.

A non-recourse loan is secured by the investment itself: the real estate purchased in an IRA. In the event of foreclosure or default, the lender can only pursue the IRA asset, protecting the IRA holder's personal savings and other assets.

Because of the increased risk, non-recourse loans come with stricter criteria (the property must have strong income potential) and higher interest rates compared to traditional loans. These loans are not offered by most banks. You need an IRA non-recourse real estate lender.

Understanding Recourse vs. Non-recourse Debt

When considering an IRA loan, it's important to understand how you're liable for repayment. Traditional loans are considered recourse debt. This means if you default on the loan (fail to make payments), the lender can go after your personal assets to recoup their losses. This could include your car, savings, or even your home.

In contrast, non-recourse debt, also known as non-recourse financing or qualified non-recourse financing, offers limited liability. With non-recourse loans, the lender's ability to collect is restricted to the specific collateral used to secure the loan.

In the context of real estate investments in an IRA, this typically refers to the property itself. If you default on a non-recourse loan, the lender can only seize the property, leaving your personal assets protected.

How Do Non-Recourse Loans Work?

Here are the steps on how non-recourse loans work for IRA real estate investments:

1. Choose your investment property:
Research and identify real estate that aligns with your investment goals. Remember, most lenders prefer properties with strong rental income potential, like multi-unit buildings.

2. Establish a self-directed IRA:
Not all IRAs allow alternative investments like real estate. You'll need to open a self-directed IRA with a custodian who specializes in real estate IRAs. Bring funds from another IRA or old 401(k) to your self-directed IRA.

3. Secure non-recourse loan approval:
Find a lender specializing in non-recourse IRA loans. They will assess the property, your IRA's eligibility, and your loan options. They will also determine the amount your IRA will need as a down payment. Be prepared to provide detailed information about the property, your investment plan, and your IRA's holdings.

Your credit history isn't a factor. The loan is made directly to your IRA, not to you.

4. Close on the property:
Once approved, your IRA custodian will handle the transaction and work with your loan provider. Some of your IRA funds will be used to make a down payment on the property. The non-recourse loan will cover the remaining purchase price.

5. Manage your investment property:
The property's rental income is deposited into your self-directed IRA. This income helps with the non-recourse loan payments over time, building equity within your IRA. All rental income and expenses (such as property taxes) for the property flow through the IRA.

In the event of default or foreclosure on the non-recourse loan, the lender cannot take legal action or go after the IRA owner's other assets. The IRA account holder is not personally liable.

Finding Non-Recourse Loan Providers

Most banks do not offer non-recourse loans. You must shop around for a non-recourse IRA lender, as every lender has different requirements, restrictions, and terms. Here are some basic questions to ask when researching non-recourse lenders:

- What are the terms? Do they change?
- What is the loan-to-value (LTV) ratio?
- What is the loan amount?
- How is the cash flow projection calculated?
- What is the formula used to calculate this projection?
- How are loan defaults handled?
- How is rent determined?
- Are personal credit checks required?
- What are the fees? How are they charged?
- Am I limited to certain types of real estate?

Typical Fees

As with any other real estate purchase, there are closing costs. These costs must come from the IRA and not your personal funds. You can request an estimate of potential costs from your lender in advance.

Also, there will be transaction fees from your custodian for the purchase of the investment and loan. Besides fees, other factors to consider when obtaining a non-recourse loan are IRA taxes, including unrelated business income tax (UBIT) and unrelated debt-financed income (UDFI) tax.

5 Tips to Get Started with a Non-Recourse Real Estate Loan

We always recommend that you open and fund your self-directed IRA before you apply for a non-recourse loan. Moving funds from one custodian or financial institution to another can take time and may delay your purchase.

1. Open and fund a self-directed IRA. You will need to provide the lender a statement for your IRA. That's why it's important that you do this first.

2. Determine your self-directed IRA investment strategy. Will you need to bring in partners? Are you using an IRA LLC? Are you investing in residential properties or commercial properties?

3. Find a non-recourse lender and negotiate the loan agreement. Remember, this is a loan to your IRA—therefore, once you have approved the loan terms, IRAR Trust signs all documents on behalf of your IRA. You do not sign the loan documents.

4. Once your deal has been funded, set up payments to the non-recourse lender from your IRA, not from your personal bank account

5. Understanding UDFI is crucial when considering non-recourse loans for your Self-Directed IRA. Consulting with a tax advisor can help you determine how UDFI might impact your specific situation and how to optimize your investment strategy.

For investors seeking to diversify their retirement holdings and unlock the wealth-building potential of real estate, non-recourse loans offer a strategic and potent tool for financial growth and security. By harnessing the unique advantages of non-recourse financing, you can mitigate personal liability while tapping into the potential of real estate assets.

About IRAR Trust Company

IRA Resources, Inc. (IRAR) is a custodian and administrator for self-directed retirement plans. For more than 30 years, IRAR has been in the industry, placing high value on first-hand personal service at a cost-effective price for its clients.

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