



## 10 Pros and Cons of Self-Directed IRA Real Estate



[Self-directed investing](#) is a great way to take control of your freedom and invest in assets you trust. While there are many different assets to explore, real estate remains one of the most popular options.

Between its high-growth potential and steady earnings, purchasing real estate with an IRA could be your early ticket to retirement.

Understanding the benefits and potential drawbacks of using your SDIRA to invest in real estate is an important part of developing your investment strategy.

## How to Invest in Real Estate Using an IRA

Unfortunately, most [retirement plans](#) restrict your ability to purchase real estate, aside from REITs and stocks.

However, a [self-directed IRA](#) enables investors to tap into alternative assets, like real estate—though there are some exceptions.

Property purchased via an IRA can only be used for investment purposes and cannot be used to house you or your family. Additionally, you need to hire a professional to work on your property, as you can not make any modifications yourself.

Once you've opened your SDIRA, you will need to fund it with cash. Most SDIRA real estate investments require a cash purchase, so you must put in enough money to buy your target property.

After you purchase the property, you'll need to file the necessary paperwork through your custodian, and your properties will show up in your SDIRA account.

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## What Types of Real Estate Can I Hold in My IRA?

SDIRAs can be used to purchase virtually any type of real estate, including:

- Vacant land
- Single-family properties
- Multi-family properties
- Commercial properties
- Real estate development companies

Again, it's important to note that these properties are used for investment purposes only.

As for tax purposes, your custodian will need to file Form 5498 yearly to report your investment properties' fair market value (FMV). For this reason, it's important to choose a [self-directed IRA custodian](#) you trust.

With this information in mind, let's explore 10 pros and cons of investing in real estate with an SDIRA.

## 10 Pros and Cons of SDIRA Real Estate Investing

### 1. Pro – Tax-Free or Tax-Deferred Account Growth

There are several tax advantages of investing in real estate through your SDIRA. For example, tax-deferred or even tax-exempt investments allow you to keep more of your money in your pocket.

So, in addition to taking advantage of the 1031 exchange loophole, you can also liquidate your investment in the future tax-free if you have a [Roth IRA](#) structure for your SDIRA.

### 2. Con – Unrelated Debt-Financed Income

UDFI can occur when any property held produces income. As a result, any gains from that property may be indebted at any time during the tax year, creating an additional tax burden. However, this only occurs in certain cases.

For example, if you use a loan to purchase property for your SDIRA, the income for your property would be subject to UDFI. Unfortunately, if you don't have the money upfront, you may have to deal with penalties that eat away at profits.

### 3. Pro – Control over Your Property Choices

Having greater control over your investments is the primary reason for choosing an SDIRA. Determining the types of properties you want to invest in gives you complete control over your retirement funds and opens up higher growth potential for your account.

### 4. Con – Fluctuating Market

The real estate market can be particularly volatile, especially as interest rates fluctuate. Many external factors impact local real estate markets, so you will need to be prepared to endure some bad times. However, real estate markets always present opportunities for investors—if you know where to look.

### 5. Pro-Protected Investments

Self-directed IRAs are protected from creditors, which is great news if you experience any financial setbacks. While bankruptcy is never desirable, there are times when bankruptcy protection can protect you. Thankfully, should that happen to you, you can rest assured knowing your SDIRA investments are protected.

## 6. Con – Pricey Investment

It is not surprising that purchasing real estate is expensive. Even if you purchase property at a low point, it will still put a dent in your wallet. Including the costs of all the closing fees, upgrades, taxes, and upkeep, real estate could get very pricey.

## 7. Pro – High Return on Investment

Nevertheless, high risk confers high reward. More than 90% of the world's millionaires have real estate somewhere in their portfolio. This is primarily because real estate provides such high returns on investment. While the initial cost of investing in real estate is high, the potential returns are even higher, which makes it a desirable investment vehicle.

## 8. Con – Third Party Involvement

To take advantage of the SDIRA benefits, the IRS requires the involvement of a certified IRA custodian to hold the account. As a result, any investments must be approved by your custodian—including the release of funds.

The custodian is also responsible for tracking your account transactions to report to the IRS. Unfortunately, this may slow down your turnaround when you need to have cash at your fingertips.

Getting “checkbook” control with an LLC account is possible, but you still need to report your transactions to a custodian. Fortunately, Horizon trust works with its customers to ensure they meet proper regulatory compliance while giving them control over their investment decisions.

## 9. Pro – Opening an LLC

By opening an [SDIRA LLC](#), you can gain checkbook control and skip the middleman! Transactions won't wait on administrators; you can purchase whatever you need using your IRA fund.

As a real estate investor, you may have to act fast on a purchase or be able to have access to your funds quickly. Thankfully, having a [checkbook LLC](#) gives you that freedom and flexibility you need to act fast.

## 10. Con – Restrictions and Possible Disqualification

Taking control of your investments requires great responsibility. Not only do you need to do your due diligence on any properties you invest in, but you will also need to make sure that you're educated about requirements set forth by state and federal government entities.

For example, you cannot dwell in any property you own or make improvements with your own hands. Knowing how to navigate the requirements while also making informed investment decisions can be a major undertaking.



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