**EPISODE 1155**

**[INTRODUCTION]**

**[0:00:01.6] ANNOUNCER:** Welcome to The Real Estate Syndication Show. Whether you are a seasoned investor or building a new real estate business, this is the show for you. Whitney Sewell talks to top experts in the business. Our goal is to help you master real estate syndication.

And now your host, Whitney Sewell.

**0:00:24.0**
**Whitney Sewell (WS):** This is your Daily Real Estate Syndication Show. I'm your host, Whitney Sewell. We are introducing a new segment called The Real Estate Syndication Show Highlights, where we're bringing you a look back at episodes focused on a specific topic that we believe added a lot of value to you in your syndication journey.

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[INTERVIEW 1]

**00:00:50.0**
**Whitney Sewell (WS):** Our guest is Dave Foster. Thanks for being on the show, Dave.

**00:00:52.0**
**Dave Foster (DF):** Hey Whitney, it's great to be here with you today.

**00:00:54.0**
**WS:** Could you give us a little background on how you got into the 1031 business? Or being that qualified intermediary?

**00:01:01.0**
**DF:** 1031 exchange is a process. It's been a part of the tax code for 100 years, since 1920. Originally, what you had to do was swapped properties and actually with someone else. It was designed for farmers and operators. Well, you can imagine in today's market how tough that would be. The core case that was settled, allowed investors than to simply sell real estate that they held for investment and purchase many real estate that they held for investment and they did have tax in the middle. As soon as I saw tha, the light clicked on. I said, "oh my gosh, this

is it, I can't continue my practice exactly how I do it, but as long as I'm using 1031, I get to use the tax dollars to build my portfolio as well."

So that was the start of everything. The start of me doing 1031 exchanges for myself, and I had some friends that said, "Dave we're setting up a shop, won't you come in and join us?" And so looking back now, 20 years later, here we are still doing 1031 exchanges, still saving tons of tax dollars, and I did give my 10 years on this alone.

**00:02:09.0**
**WS:** So you refer to yourself as a qualified intermediary. Can you tell us, how do we find somebody like yourself and how do we know that they are technically qualified? Somebody that we wanna work with?

**00:02:19.0**
**DF:** Yeah, well, first of all, the qualified intermediary is a requirement for a 1031 exchange. You must use the services of an unrelated third party, the only role that we fill in your transaction is the documentation and the process of your 1031. So the investors use all of their professionals -- realtors, attorneys, accountants, title companies for their transactions. The qualified intermediary is a third party that handles just the 1031 portion of that transaction. And Whitney here's where the other shoe drops -- a qualified intermediary, in IRS speak, only means that I'm not disqualified and I'm only disqualified if I have relation to you, or if we have a partner of the business relationship.

So a qualified intermediary, although it sounds very noble, I'll take the title, it really just means that I'm unrelated to you. So your question about how do we know who are trusting or does this person know what they're doing isn't so simple as looking for who is qualified. You've got to vet that person to see what kind of real background that they've got, demonstrated experience ,and safe cards for the customer. Honestly, most qualified intermediary firms that we do are made of attorneys and accountants. There are attorneys that will do a few every year, and maybe accountants do a few for a year. But they're never going to do this for their clients.

So it is a kind of that you gotta do a search to find it, but there's a few of us out there -- the national firms. That's all we do.

**00:03:57.0**
**WS:** That's interesting. And before the show, you and I are talking a little bit about this, and I really like to focus on that investor that is probably listening that maybe has a few rentals and they're looking to get into either syndication business, but really maybe they wanna go even passive or just that life stock of an investor that you and I discussed.

**0:04:14.9**
**DF:** Absolutely, I've got a theory. I don't know how I would ever prove it or not. But my theory is that more people enter into real estate investing because they get married than any other reason. I have no clue how I can prove that. We all know that we're getting married later and later in life. And so when two people get married, so many times he's a house and she has a house and they move into one of them as part of their marriage and guess what they just become? Real estate investors 'cause they still got the other house. And I see in time after that, we call an accidental investor, but it's kind of like a drug that gets into your system -- the real estate investing thing. You get a monthly rent coming in. That's kind of a cool thing. So over time, what do we do? We want more and more of it. So we start buying more properties, more properties, more properties. And that's a great way to use the 1031 exchange because when you sell, say a $200,000 piece of property, you can use the proceeds to go by two $100,000 pieces of property. So you can diversify more quickly. So 1031 really helps to build.

And we offer investors doing that quite a bit. But sooner or later Whitney, one day you wake up tired and you don't know why until the first phone call that day comes from the tenant with the plumbing issue. And the second phone call comes from the tenant who fell off the ice in front of your house. And the third call comes and you go, "Oh, that's why I'm tired. I've got 20 different rentals here. And it's killing me, and I did this so I could enjoy life."

So again, the 1031 exchange can't be used to do what we would call consolidating our portfolios. So two properties each for $200,000 and go buy one property for $400,000 and start to narrow your horizon, start to minimize the cost and the effort of management instead to give it to yourself. A debit flow is what we call the life cycle of a real estate investor. It starts out with only more, more active, and then as you get towards the latter stages of it, the focus becomes on minimizing distractions, maximizing passivity and creating income streams, and (inaudible) the latter are not gonna require you. And that's kind of the world where you and I both live. From the 1031 perspective, it involves selling to position assets of the syndication side, that's one of the types of assets that can sometimes work.

**00:07:02.0**
**WS:** So let's focus on that person who has, whatever their portfolio is, maybe they've built it to 100 single-family homes, and now they've said, "Okay, you know, I've had enough of this and I wanna just invest in somebody syndication as a limited partner." Can they use 1031 to do that?

**00:07:20.0**
**DF:** Sure, yeah. Well, that's kind of the cross where we give to what the big problem. The big issue, the roadblock is in that because we're 1031, you can use it to move into different properties, hire property managers who you can just fire. But sooner later you realize you're

having to manage property managers, that's not so much a plan. You can take on the 1031 exchanges, if you could move into things to fix assets that are triple their commercial assets, where the tenant pays all of the taxes, insurance, and maintenance, that's a very impressive way of investing. The problem is, the price tag on those can be very, very high. You can also go into a set of relatively new classes that lasts 15 or 20 years, which are fractional, passive commercial investments. Triple net leases, where instead of having to buy the whole building, you're buying a part of that building. And that can accommodate 1031 investor who doesn't have a pull-out necessary. The key in all of those scenarios is that the investor is selling real estate and actually buying real estate, even when it's fractional ownership, they're buying a tenant in the real estate itself and that's what makes it work with 1031. You have to sell real estate. You actually have to buy real estate.

So there's the problem with syndication. Most with actually 1031 were syndications. Most syndications, the way they are set up, Whitney by the way, you have been doing this for very long, 'cause you look like you're about 20 years old, but back in the old days, syndication was kinda used in all out of different ways. We call them partnerships. We call them joint ventures. The pure idea of syndication isn't anything necessarily new, but what is new or relatively new is the new structure that syndication is being created with. And most of them are going the legal route of limited liability partnership with a general partner and limited partners. Some are being done as LLCs as well. Now, we're doing that for a ride of security, financing, most with valid reasons. But what that's done now is it's put a limitation on a 1031 investor.

In the old days, if I wanted to create two-person syndication, I would simply have the other investor and I purchased the property together as tenants. With the new structure syndications, they're being set up as limited partnerships. What I have to buy is not the real estate itself, I'm buying the membership interest, and the entity is real estate.

Unfortunately, that doesn't qualify for 1031. So 1031 investor has a couple of options that they can look at. Certainly, they can say, "You know, well, I've had a good renter, maybe it's not to sell this one. Pay a little tax and go into syndication with by now tax-free dollars." And that can be a good avenue to do it, particularly if you've got a sharp accountant and you could work with Dave and say, "Oh, here are some capital loses, we can offset that with..." Now, we're gonna make this work. You have capital losses, so it's not a strategy I recommend. But it will work.

[INTERVIEW 2]

**00:10:41.0**
**WS:** I'm excited to have Dave Zook. He's a successful business owner. He's an author and speaker. He owns approximately 3,000 units. He got in a multifamily real estate 'cause he had a

tax problem. He's experienced on the passive investor side, and also as a syndicator. I'm thrilled to have him on the show. Thanks again, Dave.

**00:10:57.0**
**Dave Zook (DZ):** Whitney, hey, thanks for having me on your show.

**00:10:59.0**
**WS:** Dave would you give us a little about your background and how you got into multifamily syndication?

**00:11:03.0**
**DZ:** Yeah, so I, early on, I was very intentional I was not gonna be a real estate investor and simply for the reason that I saw my dad invest in real estate and self-manage some of his single-family homes, and I just thought there's gotta be a better way to make money than that. So I specifically steered away from real estate and I invested, although I was an investor and business owner from my mid to late teens ever since, I invested in the business. And I started a couple of businesses, I partnered with people with businesses, and I sold a business or two and got to the point where I started making a lot of money with these businesses, and they were doing really well and got me into a situation where I was paying almost a half a million dollars a year a tax. And I got tired of it. And so through listening to Robert Kiyosaki, reading his stuff, and then I eventually get to the point where I realized that real estate was not only had a lot of other really good benefits -- tax protection was the big one.

So for me, when people ask me and I got into real estate, I always say I was chased into it for a tax reason. I was paying a lot of tax and I recognized after a while that real estate, specifically multifamily real estate, can be a real tax shelter. So I really got into it for the tax protection pace.

**0:12:31.3**
**WS:** Nice. Can you tell us what some of those tax shelters or tax benefits that you were looking for? You were that pie income earner. What were you looking for exactly in the tax shelter? Can you explain a little bit of that?

**00:12:41.0**
**DZ:** I'll just give you an example. We get very strategic on the tax side now, and I've learned a lot in the last decade. So we'll go in and we'll buy a multifamily apartment building, we'll do a cost segregation study, we use bonus depreciation that's now available to us as of the end of last year, and there's just some incredible tax incentive there for real estate investors. And so for me, when I go and do my tax planning and I go looking toward the end of the year and I

have an option, I'm either gonna stroke a check for a big tax bill or I'm gonna invest in an asset that gives me the tax protection, which ones are gonna be?

Well, for me, that's pretty easy. So I'll just give you an example, we bought a 138-unit apartment building late last year. And we were able to use the additional tax benefits through the bonus depreciation plan that they came out with at the end of the year. And they then rolled that back to September 27. So anything we bought between number 27th and last year, at the end of the year, we were able to use this bonus depreciation rule. Well, an investor who invested with us through one of our syndications and invested $100,000 into the deal, they got $91,000 in tax deduction back. So just incredible what you can do with a little strategy, with some good members on your team to be able to make that happen, it's incredible what you can do to save on your tax liability when you use the little strategy.

**0:14:12.9**
**WS:** Wow, that's incredible. $91,000. So let's go back a little bit, when you were that passive investor or high-income earner, how did you get started then, how did you know who you wanted to invest with? You wanted to stay away from real estate initially, but then you see these benefits and how did you know who you wanted to invest with?

**00:14:28.0**
**DZ:** Get around different events, get around different people, getting around people with connections. I gotta tell you, as a passive investor, it hasn't always worked out really well. The very first passive investment deal in a big multifamily apartment building, I end up up to lose in a couple hundred thousand dollars just simply because I had teamed up with the wrong guy.

So it doesn't always work out well, but that's a big part of that, you gotta pick your team wisely. And if you don't, it can cost you big.

**00:14:59.0**
**WS:** What was it about that team member? What should we be looking for so we can avoid that same situation if we're passive investors?

**00:15:06.0**
**DZ:** We talked a good game when we go to a sales guy. But his competence in running an apartment building wasn't that great. So I mean, I made a bunch of mistakes. It was early on, I got excited about this deal, I got sold this deal, and this was gonna be the greatest thing ever, and it was gonna be a home run right out of the park. Well, I ended up being the only syndicator in the deal. And I brought to $750,000 to the deal and ended up going home with just over $250 a little while later, a couple of years later. So number one, it was the first field that I'd ever done with this guy, I should have maybe just started with 50 or 100,000 or really

watched him perform with a little bit of money instead of going all in. And so that was one of them. There were other mistakes that, there were other things that I learned throughout that whole process that was the big one, putting all the eggs in that basket and getting excited about the deal, letting your emotions take control ahead of logic. So it was a lesson well learned, it was an expensive lesson, but now looking back, I'm glad I went through it and it's made me a better investor.

**00:16:19.0**
**WS:** Awesome. I'm glad you can see that side of it now. You talked about watching him perform with a little bit of money before going all in, and I think that's some great advice. I've heard numerous passive investors talk about how they'll do a little bit, you know, numerous syndicators deals just to diversify. And is that something you recommend now, or how do you handle that? To keep that from happening again?

**00:16:37.0**
**DZ:** Yeah, and it's the same with asset classes as well, different asset classes. And let's say you start with, say, three or four or five, and you try to figure out, "Okay, what asset class is I most fond of?" You know it could take a year. Do you see your K1, your tax benefits on each one, and then you can go back the next year and invest heavier in the ones you want. Same with a promoter or a sponsor. I've got investors who do the same thing, they'll invest with me, they'll invest with or three other guys. And then eventually it gets to the point where they just invest with me, and we do deals over and over again. I got guys that invest with 10, 15, 20 different deals and invest any deal that I do. And that, of course, doesn't happen the first time around, you don't get that right out of the gate, but you get that from years of performance and you build up that trust level and you show that you're competent, and you show you can get the deal done, do what you say you gotta do.

[END OF INTERVIEW]

**00:16:59.0**
**Whitney Sewell:** We hope that you enjoyed the Highlights show today. You can always listen to the full episodes that were featured today by clicking the links on the show notes page. and in the description box. Let us know what you've thought of this episode or you can go to [lifebridgecapital.com/podcast](lifebridgecapital.com/podcast) and click the feedback button. Let us know how we can add more value to you. Thank you and talk to you tomorrow.

[OUTRO]

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