EPISODE 1560

[INTRODUCTION]

Whitney Sewell (WS): This is your daily Real Estate Syndication Show and I'm your host, Whitney Sewell. Today we have packed a few different shows together that we call Highlights to help you to get the most bang for your time and educating you on the topics that you want to learn from. We would love to hear from you. I am grateful that you are with us today. Have a blessed day.

[INTERVIEW]

WS: Our guest is Brett Swarts. Thanks for being on the show, Brett.

Brett Swarts (BS): Whitney, thanks for having me.

WS: Now, I'm honored to have you on the show. You have some skills that we need to know. You have a specialty here that I'm looking forward to getting into today.

But a little about Brett, he's the CEO of Capital Gains Tax Solutions, and every year equips hundreds of business professionals with a Deferred Sales Trust tool to help their high-net-worth clients solve capital gains tax-deferred limitations. His experience includes numerous Deferred Sales Trusts, Delaware statute trusts, 1031 exchanges, and $85 million in closed commercial real estate broker transactions. An active commercial real estate broker and investor himself with experience and holdings in multi-family, senior living, retail, medical office, and mixed-use properties. He's a licensed California real estate broker and holds Series 22 and 63 licenses. He formally was an associate at the largest commercial real estate brokerage firm in the country.

So, Brett, thank you again for your time being on the show today. Give the listeners a little more about who you are and exactly what we're going to talk about today.

BS: Yeah, thanks. Thanks, Whitney. Yes. So I live in Sacramento, California. I have five kids with my wife, Melanie. We've been married 10 years and we kind of grew up in native California. Originally from Mission San Jose Bay area, where I learned, kind of, the real estate world with my dad, building custom homes. The majority of my time, actually, in Rockland, California, which is in Sacramento. I played sports in high school. I played basketball in college and learned about investing in real estate in 2006, and kind of haven't looked back. It's been my passion. I love helping people create and preserve more wealth through passive and/or active investment real estate holdings. So I learned about a tax deferral strategy along the way. Now,

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we want to empower business professionals like yourself and others to help people defer tax and do more deals.

WS: So you are going to help us to defer tax. I mean, that sounds pretty good. That sounds pretty good. As a syndicator in the syndication business, just get us started in some things we should be thinking about and what this means for us.

BS: So, most commercial real estate syndicators, they have partners and even themselves, they struggle with capital gains tax and depreciation recapture when they go to sell their high-end primary home, business, or commercial real estate. We use a Deferred Sales Trust, which is just an installment sale, creative installment sale, to give them tax deferral, liquidity, diversification. The best thing is the ability to buy or invest into other commercial real estate deals at optimal timing, so that they can create and preserve more wealth, and as a commercial real estate syndicator, so that you can add massive amounts of value to your partners, and so that you can create and preserve more wealth and attract more capital. Well, a better way to put it is: unlock the capital that is stuck in an illiquid asset.

So to give you some more context here, according to the American Bankers Association, there's about $17 trillion that will pass from one generation to the next in the next 20 years, and this is known as the largest vault transfer in the history of the planet, and this is by the baby boomer generation. In fact, alone in America there's about 77 million baby boomers, and every day about 10,000 of those turn 65. What's happening with them? They feel really trapped. We call it the perfect storm. They're trapped because they want to get out of the toilets, the trash, and the liability. They want to able to maybe retire from the active management of commercial real estate and be more passive with a syndicator who perhaps is a little bit younger and is maybe in a different geographical location, and has some value-added force depreciation opportunities versus their one particular town or city that they're in.

The next thing has to do with just interest rates that are hovering near 40-year lows, and real estate business appreciating a great deal. We call this the perfect storm of what do you do, and how you help that group to diversify and get liquid, and then be able to invest in deals that you have lined up.

WS: 77 Million baby boomers and you said 1.5 million turning 65 every day.

BS: 10,000 Turning 65 every day.

WS: 10,000?

BS: Yeah.

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WS: I was like, “What!” 10,000, Okay. Then interest rates or 40-year lows. So get us started as far as what this means for the syndicator, what we should be doing or thinking about or how to understand how to use a vehicle like this.

BS: Yes. So most of you and your listeners, and I know you know about the 1031 exchange, which is a tactical strategy for investment real estate, for lifetime real estate. You know the value of that, because essentially you can defer the tax and roll it into a deal and keep that growing your wealth, versus paying the tax, which is about 30 to 50%. That’s usually what we’re working against. 30 to 50% Of every deal that’s sold is going to have a capital gains tax, state, federal, Obamacare, and then plus depreciation recapture. Instead of paying that, you do a 1031 exchange. But the challenge with most syndicators we work with, or operators, is a lot of them don’t allow exchanges into their deals unless there’s a certain deal size. Also, on the flip side, when they go to sell, everyone is just paying their tax.

So into the Deferred Sales Trust, the intent is to defer the tax. The problem is there’s not a clean or concise way to make it happen with the 1031, whereas the deferential trust is very flexible. Each partner can go their separate ways. It also works – They can have their own Deferred Sales Trust. Or they can just pay their tax or do a mixture of both, and then invest it into your deal. The next thing has to do with timing. In a traditional 1031 exchange, you have to do something within 180 days. Meaning you sell and buy something within 180 days, and identify within 45. So the intent again is to find a deal. But the problem is, especially if it’s a highly appreciated marketplace, especially in properties they’re selling, it’s difficult to find a deal within a certain period of time, whereas the Deferred Sales Trust is a solution for this, and that you can put the funds into the trust and you can buy whenever you want to. Meaning optimal timing, tomorrow, day 181, five years from now.

Part of what happened in the ’08 run up, Whitney, and I witnessed this firsthand, especially in Sacramento. It was one of the hardest hit cities in America. It was people were selling real estate ’04, ’05, ’06, ’07, and they were 1031 exchanging into bigger and bigger properties. The challenge was they were overpaying a lot of times because of the tax. We say, “No, there’s a better way to do it.” You can actually get out of debt, and also that’s with the 1031 – Oftentimes, it forces you to do, to stay in debt, or take on more debt because of equal or greater value rule. Instead, put it all to the Deferred Sales Trust. Now, you’re liquid, you’re diversified, and then you can go into multiple syndication deals across the US, smaller amounts.

So It’s just a more flexible way to defer tax, and then again for the syndicator to unlock that capital for folks that want to sell that business. We’ve done thousands of these transactions with veterinarians, dentists, doctors, tech companies, apartment complexes, self-storage. They

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want to attract that high-net-worth. But a lot of those clients, they feel trapped in those properties and they don't want to do another 1031 if its investment property. But they love the Deferred Sales Trust to unlock that capital, so they can deploy into your deal tomorrow.

WS: So can you walk me through an example? When would something like this apply? How do we get it started? Where are we at in the process of the property and selling and buying?

BS: Yes. Let's walk through an example. So I just did a recent deal in Sacramento. It's a $1.8 million sale for a gentleman named Peter. He was turning 70. He's at Marin, California. He's driving to South Sacramento to manage 18 units. It's one of those deals where it's kind of hard to hire management because it's not that big. If you do, it takes a lot of the profits away. So he's doing a lot of it himself, and he's always been a hands-on guy too. So he's on multiple 1031s over the years. So he has not only debt on the property, but he also has a big capital gains tax of 500,000. He told me, "Brett, look. I don't want to trade 18 problems for 36 problems. I made my wealth. I don't need any more of these headaches." I mean, he's banging on doors, trying to collect rents, making evictions. He's just gone, "I want to be done. But I also don't want any more debt , and I don't want to overpay."

So enter the Deferred Sales Trust, he sold it, moved all the funds into the Deferred Sales Trust, paid up all of his debt, and deferred $500,000 in capital gains tax. Here's the biggest reason why. He said, "Brett, I want to buy, or partner with people who are operators anytime, tomorrow when the deal comes up." He thinks the market's going to shift another one or two or three years, and that's when he's going to be poised to strike. In the meantime, he's invested in stocks bonds, mutual funds, diversified, liquid, conservative stuff. Nothing that's too much stocks, and he's just keeping his powder dry.

So it comes up in those scenarios from the gentleman who's older, who wants to diversify, who wants to retire. For the syndicator, it comes up, because again we're looking for ways to attract and unlock wealth to invest in our deals. So the way we do that is we provide the solution for folks, the solution to be able to do that. So again, if it's a business, if it's artwork, if it's a collectible, the Deferred Sales Trust works for all of those. 1031 is very specific. It only works for investment property. So, that's where it falls short.

The other part is for the people you're actually buying from. So now, I want you to put on the actual syndicator I'm looking for to find the deal and who's the ideal person to buy from? Well, it's the mom-and-pop who's kept the rents low, who's been very nice to the tenants. He's owned it for 20, 30, 40 years, who's fully depreciated, who doesn't want to do another 1031. They don't need more money. They get calls all the time with, "Hey, why don't you do a 1031?" They're going, "No, I've done that for 40 years or 30 years." So you want to buy it from those folks where there's a value-add forced depreciation.

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So into the Deferred Sales Trust, when you call them and say, “Hey! Look, Mr. owner, I know you don’t want to do a 1031. There’s actually a different way for you. It’s called a Deferred Sales Trust.” You’ve just solved their problem. They’re more likely to sell it to you versus anybody else. They’re more likely to sell off-market to you versus anybody else. They’re more likely to take a lower price. Why? Because they’re going to save 30 to 50% on their sale, and they’re going to be liquid, they’re going to be diversified, and they’re not going to have to do the active real estate.

So I’ll pause there, because I know I just said a lot. It’s probably – Maybe some questions you have.

WS: Yeah. So I was thinking about – So go back to the first example. So, the guy that sold the 1.8 million. So he sells that. He puts all of that in a Deferred Sales Trust. So now, he can invest it however he wants, right?

BS: Yeah. There’s only two exceptions. You can’t put into a primary home and you can’t go overseas. But it can go into investment real estate with up to 80% of the funds. The remaining 20% will stay in stocks, bonds, mutual funds. But it can also go into a business startup. As long as there’s business, purpose, and investment to be made in the US, yes.

WS: But he did have to pay some capital gains or he did not?

BS: No. 100% deferred. Yeah, he put all the proceeds in there, so he’s 100% deferred.

WS: So when will he pay taxes?

BS: Good question, Whitney. When would you like to pay taxes? So most of our clients like to pay the taxes second day to never. Meaning, they’re just going to live off the interest, so they’re going to keep 1031-ing, and just keep doing that. So the moment he takes boot, or the moment he receives actual receipt of the cash, this is when it’s triggered, which is how this works, which by the way it’s how a 1031 works.

So let’s walk through how this kind of works, Whitney. All right? So you ready? You’re going to be the seller, and I’m approaching you. So, Whitney, you’re selling a $10 million deal. It has a zero basis. You have no debt. If you were to sell today, you would owe, let’s say, four million in tax. So you definitely want to do a tax deferral strategy, because those numbers are pretty brutal if you get taxed. So I approach you as just the regular person off the street and say, “I’m going to buy your apartment complex, Whitney. May I give you a $2 million downpayment. Would you please carry a note for eight? Would you do a seller carryback?” Let’s just say you

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say, “Yes.” So on that scenario, Whitney, if I give you $2 million down, how much actual receipt did you receive?

WS: That’s what – Yes.

BS: So you’re going to owe tax on that two, because that’s what it’s triggered. But the other eight million is what’s called a seller carry-back. It’s in a deferral state. Do you follow?

WS: I am.

BS: Now, what if I sell? I’ll give you a zero down payment, Whitney. If I give you a zero down payment today and you carry a note for 10 million, hypothetically you wouldn’t do that, because in a real world, [inaudible]. How much tax would you owe if I give you zero down payment today?

WS: None.

BS: Zero, because you haven’t received anything, and the other 10 million is in a deferral state. Now, that income or the interest is going to happen, and I’m going to pay you interest, and you’re going to pay ordinary income on that interest. So that’s how a Deferred Sales Trust works. Here’s the difference. We have this $10 million buyer lined up, and we have Whitney ready to sell. They’re about to do the transaction. But what happens is the trust jumps in right between, and it actually buys your position for 10 million in exchange for an installment note. It gives you a note. It gives a zero down payment exchange for the property and immediately turns around the same [inaudible] and sells it to that buyer. That buyer puts the 10 million into the trust. So if the trust bought it for 10 million and sold for 10 million, how much gain does the trust have?

WS: Zero.

BS: Zero. You got it. Whitney, again if you took a zero down payment in exchange for the note for 10, you’re in the deferral state. So how much do you owe today?

WS: Zero?

BS: You got it. So the buyer takes the title. He’s gone. So that’s how it all works. That’s why it works. If the 1920s tax law goes back 90 plus years. We’re just creative on how we apply the law. That’s exactly what the IRS said too. That’s how we know it’s legal. We have thousands of business professionals across the US. But all that being said, what it does now for you as the syndicator or as the owner is it takes you out of those timelines of that 1031, because the tax

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law for 1031 is IRC 1031. Whereas us, for IRC 453. So these are two tax deferral strategies but have different rules. These rules for the 453 are much more flexible than the 1031, which means no equal or greater value, no short time period, no replacing of any debt of any kind, multiple product types, multiple investment vehicles, and I can go in and out of the trust, all tax-deferred, for as long as I want.

The best one I think for you guys has to do with depreciation. So in a 1031 exchange, the depreciation schedule travels. Meaning, if you take any accelerated depreciation on deals or any depreciation for that matter, and you sell and do a 1031 exchange, that depreciation schedule goes into the next deals. Meaning, you need to buy a bigger property to offset this. So let's say it was a $10 million deal again. You fully depreciated out. If you were to sell today and buy an exact $10 million deal, there's no new depreciation. It's already zero. If you buy a $25 million deal, well now you got an extra 15 million in depreciation. But that might take on a lot of debt and a lot of risks. So some people are like, "I don't want to do that."

Well into the Deferred Sales Trust, we could sell that same $10 million and put it into the trust. Use $8 million to go purchase let's say a $25 million deal. Now, there's a brand-new $25 million deal amount of depreciation. It's a brand-new schedule, because I didn't do a 1031. I partnered with my trust to purchase this. That's very powerful. So now, you can do accelerated depreciation to offset the income everywhere.

[INTERVIEW 2]

WS: our guest is Hugh Odom. Thanks for being on the show, Hugh.

Hugh Odom (HO): Thank you, Whitney. I appreciate the opportunity.

WS: Hugh is a former AT&T attorney for over 11 years and the founder and president of Vertical Consultants, telecom consulting firm that has provided consulting advice for companies like Walmart and Disney and government institutions like the United States Postal Service, New York Housing Authority and Veterans Affairs. He has been a resource and newspapers, podcast radio shows and blogs for years. He has the ability to understand the true value of land to cell tower companies as they roll out hundreds of thousands of new towers using commercial buildings. Hugh, welcome to the show. I think this is just an interesting topic. We've not talked about this on the show. Hardly at all, if at all. I can't remember the time we talked about cell phone towers, but I tell you one thing, we're all looking for ways to add more value to our property, right? And I know people who have added cell towers in some form of fashion and vary a little, but I've heard of that, and it can add value, but then again, there's a lot of things that it could trip you up with as well, just like you and I were talking about before, and so I'm looking forward to getting into that. And so Hugh, give us a

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little about your background, and let's dive into this topic of cell towers and land and the value of each of those, and maybe that's an option for us at least… Help us to know that we're doing it correctly.

HO: My background or the people that make up our companies background, we were in the telecom ministry for 10, 15 years respectively, and I was an attorney at AT&T for over a decade. When I was on the other side of the table, let's say I was the guy negotiating instructure and grievance to lease or acquire land for infrastructure for AT&T to build out our cell tower and other types of equipment. And then 10 years ago, we started Vertical Consultants.

We basically just think of us going on the other side of the table, because saw… we saw this huge difference in ability between the cell tower companies, the wireless carriers, and the landowners. The land owners were not getting valued, but as you mentioned, they are entering into agreements that have a negative impact on their land. So we started working with individuals, churches, schools, small business, from very large businesses as well, to assist them in evaluating these opportunities, but also structuring them in a way to give some value today and throughout the term, but also protects their land as well, and their building.

WS: Nice. Well, I have consultants for all kinds of things, or have had coaches and people on our team, because there's so many different aspects of business in general, especially the commercial real estate business that you can't know everything, right? That's why your team is so important, and I can see why someone would hire somebody like yourself for something like this, 'cause it seems so kind of out in the field a little bit for most of us, but it could be a great way, like I said, to add some value potentially. And so help us to think about who in commercial real estate are those prime candidates for something like a cell tower?

HO: Well, with the…we're all at a 5G. I mean, everybody's gonna be a candidate to some extent with a commercial property, but the bill at is gonna be mostly in urban areas and then also areas that are in a kind of mixed area. Well, we call that mixed area. It's a commercial residential mix, or… We do a lot of work with self-storage and hotels and things of that nature, because they're in that mixed area to some extent, but what's gonna happen and what has happened is that if you have a building and you got property, there's going to be… And continue to be a need to build out more and more cell sites, just think of it, I tell people besides air, water and food, what is the thing you relying most every day? That's cellphone – to communicate, to get information, etcetera. It's not getting less valuable in your everyday life. It's coming more valuable, and there's two types of… people think of technology, they look at 5G and or do all this technology on their phone, that's kind of like looking at the car, and we're getting about the road that it has to drive on the technology is one part of it, but without the infrastructure, without the ability to be on those buildings, to be on that land, there's no ability to use that technology. So our job is to work with those property or to understand the value of

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their land, and to get that right agreement in place, so there's gonna be a lot of opportunity now with regards to existing property or property of an existing agreements, but also a lot more build out in the future years because the 5Gs gonna need a lot more sites.

WS: How do we know if our property would be something that we should consider adding something like a cell tower to?

HO: Every week, we probably get 300 contacts from people around the country and saying, I have a great location, I have a great building, a great place for a cell site. The easiest answer is, you'll know when they knock on your door or they sent you a letter. We work with some very large companies that have a 1000, 2000, 4, 5000 commercial properties. And in that instance, if you have a large portfolio, you can go to some of the carriers and kinda work on a master agreement between the two parties. but if you own three or four properties, I tell people you don't have to chase that cell site agreement. Gonna be a long road, and you'll probably end up nowhere, but you really need to make sure the biggest thing is understand what the opportunity that not comes the door, that phone ring, that email come to drops, is that you can understand exactly not in what you're being offered, but understand what you're giving up in exchange…

WS: Okay, so let's think through that a little bit. So we're prepared when we get that phone call or email, like you said. If we receive that, a lot of us would know what to do with that, or maybe it may sound good, or maybe the cellphone provider, whoever that is, who's contacting us may make it sound very good, right? But what do we need to know? I know you've alluded to some mistakes obviously, that people can make and just say how it can affect the entire deal in such a big way, whether it's throughout the life of the deal or the sale and financing, help us to think through that and what we should know.

HO: Sure. The first thing is, when you're being approached, towards something on your property, you're being sold something. It sounds like you're getting something but you're having sold something. You're being sold the idea, "Hey, I'm gonna give you money for free. You're not using that space on your rooftop. You're not using that proportion or property". So it's kind of like you're getting money for nothing. You're not… You're getting money for your use of your property, number one. Second of all, they try to minimize the impact on your property. When you're in a cell site agreement, you're not giving them a right to a certain portion of property, but you're putting restrictions on the rest of the property and they're all using 4, 500 square feet. They're putting certain restrictions in their agreement that it impacts your overall property, so what you need to think about when you've been approached… What we tell people all the time, ask for two basic things upfront. Ask for a copy of the agreement. Just to look at that, 'cause sometimes they'll send you a proposal over their term sheet and

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they'll try to get you to focus on that, and get you to narrow your focus on the financial term for some basic terms.

HO: Get a copy of the agreement. Second, get a very simple site plan, not only where the equipment is gonna be, but also any areas of your property you're gonna need for utilities or fiber optic lines or things of that nature, so you know exactly what you're probably gonna be encumbered by and the biggest thing we tell people with regards to this is, "Don't worry about what they're offering, you understand what you're offering them. If you understand that, that's the key of the game, they want you to focus on what they're offering you, what that number is. If you understand what you're offering them, then you can negotiate based upon knowing, getting the correct value, but also putting certain protections that you mentioned that don't have a negative impact on your property with regard to future developing your property. A lot of these agreements are in there that you're committing for 20, 30, 40 years, and they can walk away at any time, but I'll just use the example, and this works in about 99% of the leases out there. If I walked up to a property owner, I said, All of you have 10 times the market value of your property, but I have one condition, just one…

HO: And I have the money right here, I need… Let's say Verizon, I need Verizon to move their equipment 10 feet and I'll give you 10 times market value. 99% of the people out there have cell site agreements, couldn't do that deal because they have no pathway to deal with the relocation of that equipment, and now they've got into a situation by the use of their overall property is subordinate to Verizons or AT&Ts or whoever use that small piece of the property, so that's a lot to know about understanding value, but it's also a lot to know about how this impacts your overall property.

WS: Some great set of thinking about right there, it may seem like a great opportunity, but you'd have to think about the restrictions they're putting on your property, no doubt about it. To make that work, to make it a win-win. What have you seen in the past work… So we don't really chain our leg to a ball and chain, so we can't sell or get financing or whatever, maybe you share with some examples of issues that people have had, and then what we should be doing about it.

HO: Well, we use two words over and over when we talk to our class about these agreements. We use structure, and that helps you financially and also helps you with the protection, but the big word is flexibility. Flexibility, because none of us out there know exactly what's gonna happen tomorrow, more or less 10 years from now. So what you need to do is think of this way. You need to think about having certain protections and certain pathways in those agreements. For example, like I mentioned, if you wanna re-develop your property, let's say somewhere down the road, you need to have the ability for them to work around you give that being the wireless carrier to work around you, and if not, then you're gonna be, again, restricted by that.

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A lot of people are in these agreements and they forget to have had that flexibility put in there, and they often say when they're negotiating that agreement, say, "Well, you know, we don't have any plans ever to redevelop this property. It's never gonna change". And I'm gonna say, "How can you predict 20, 30 years down the road? Nobody can't… And if you don't wanna re-develop it, half the guy you wanna sell it to wants to buy it, wants to do something with it and can't do it, and that hinders your ability to sell or get a higher price for your property".

HO: So that's one thing, a lot of other things out there with regards to financing, which is kind of an interesting issue. A lot of the bigger lenders are looking at these cell site agreements is not much pluses, but sometimes a little bit of a negative if they're not structured in the right way, because the lender, if he ever has to step in the shoes of the owner because of some bad situation, he wants to have the ability to freely market the property and sell it, and sometimes these agreements, if they're not structured, these cell site agreements if not structured correctly can hinder that, and then with regards to overall pricing, the additional revenue can be a great benefit you're getting from the cell site agreement. But the problem is if you start putting restrictions and restrictions and restrictions on properties, anybody in real estate knows some of the most valuable properties, I wanna have the least amount of restriction, if you can do anything with, if you start hindering that, you start hindering your ability to do things with the property, and it also affects the net value of the property going forward.

[END OF INTERVIEW]

[OUTRO]

Whitney Sewell: Thank you for being with us again today. I hope that you have learned a lot from the show. Don't forget to like and subscribe. I hope you're telling your friends about Real Estate Syndication Show and how they can also build wealth in real estate. You can also go to LifeBridgeCapital.com and start investing today.

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