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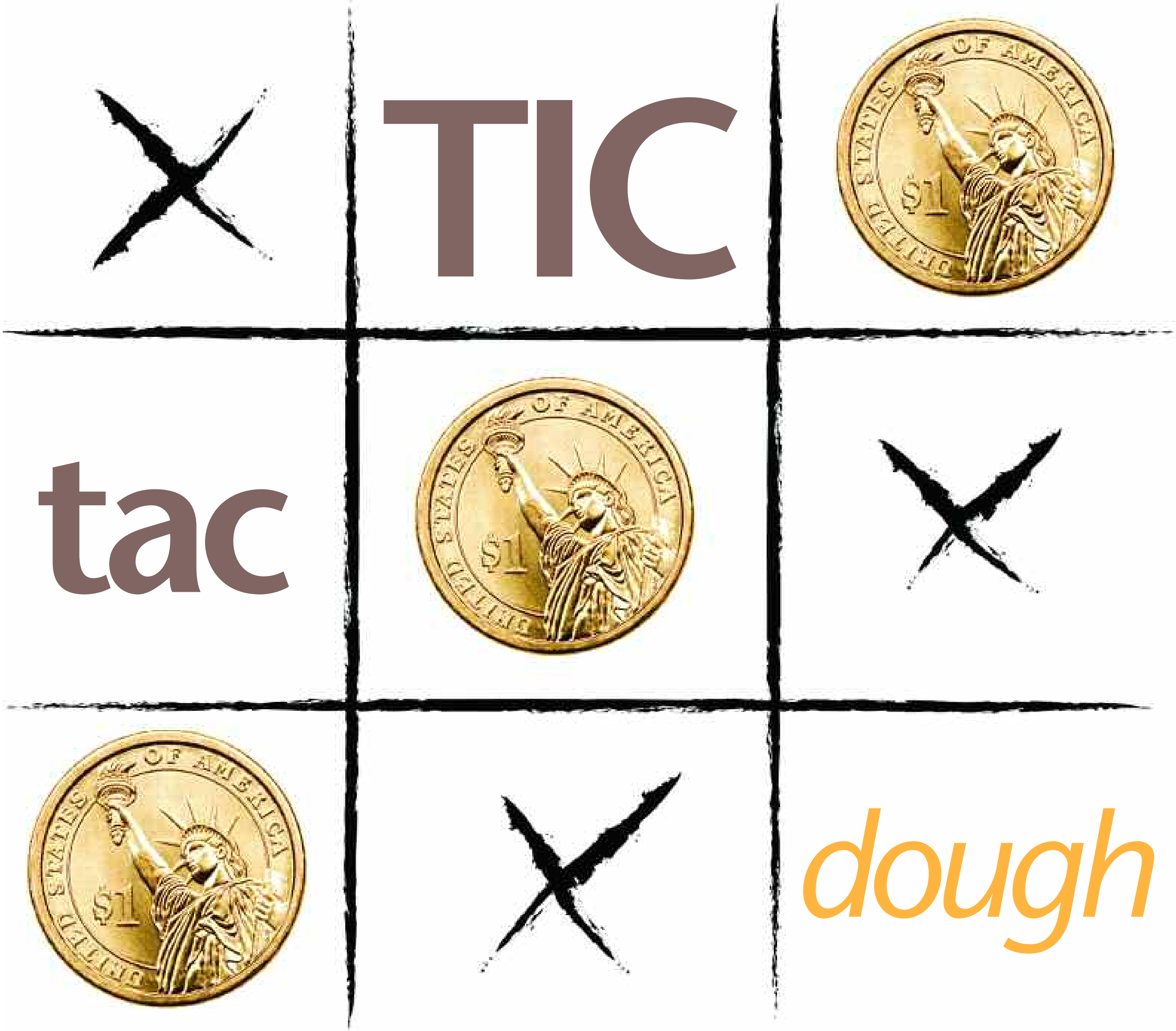

Tenant-in-common programs can keep Uncle Sam from taking a big bite out of your real estate gains.

By DAVID FISHER, Fisher Equity Advisors

In an appreciating real estate market, a 1031 exchange allows an owner of income-producing real estate the opportunity to sell his or her property and defer indefinitely the capital gains tax on the sale of that property. The IRS allows the owner to sell income-producing property and purchase another income-producing property by following several rules, and if done properly, both federal and state capital gains tax and depreciation recapture can be deferred indefinitely. Unfortunately, there are several potential obstacles to having a successful 1031 exchange.

LIMITED TIME ONLY

One of the main concerns is that once escrow closes on the sale of the property, the owner has 45 calendar days to identify a new property. Because of the supply and demand of properties, it may be difficult to find an appropriate property in a limited time span. In addition, assuming that an appropriate property is found, can it successfully be closed in time? If problems arise after the 45-day identification period is over, the sale may not be finalized, resulting in a taxable event. Other problems that may occur in finding an appropriate exchange property may include finding a property with the proper loan-to-value ratio and finding a property for the right price.

TENANT-IN-COMMON OPTIONS

There may also be circumstances where the property owner would like to take advantage of a 1031 exchange but would like to retire from the real estate market. Maybe the owner would like to replace the terrible Ts – termites, tenants and toilets – with Tahiti, Tahoe or the

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kids/grandkids. If so, exchanging for another property probably is not the best solution. For many real estate owners, a tenant-in-common program may be a viable option in a 1031 exchange.

In 2002, the IRS issued guidelines under Revenue Procedure 2002-22 governing the structure of TIC properties. These guidelines require that a TIC can have no more than 35 investors. Each individual must qualify as an accredited investor in order to participate. Depending on the circumstances, a TIC can have far fewer investors. A minimum equity amount is required for each property depending on the amount of equity needed and the number of investors.

In its simplest form, a TIC is an opportunity to purchase a fractional interest in an institutional-grade property. These properties are normally reserved for large pension funds or larger corporations. These properties can range from large apartment properties to multi-story office buildings to large industrial parks anywhere in the country. TIC properties are operated by professional property management so that investors have no direct say over day-to-day management decisions.

DIVERSITY AND DUE DILIGENCE

Using a TIC as a replacement property in an exchange offers numerous potential benefits. A TIC will provide the investor with the opportunity to invest in institutional properties that might not otherwise be available to an individual. Advantages of institutional properties include lower cost of financing and professional management. Also, institutional properties allow for the opportunity to diversify across different types and sizes of properties as well as to invest in real estate in different parts of the country. The potential advantage is the realization that a real estate slowdown in some parts of the country may not affect other parts.

Another advantage of a TIC is the due diligence that takes place by the real estate company and other financial institutions. Institutional properties usually require far more due diligence than the majority of smaller properties. Thus, the real estate sponsor and the other institutions involved spend a great deal of time and effort reviewing all aspects of each project. This would usually include the review of rent/tenant information, insurance and future projections that might affect the viability of the specific property, including population demographics and various potential economic impact studies. In addition, after these properties are underwritten by these institutions, they are again diligently reviewed by independent outside firms in an attempt to fully disclose all potential risks to the investor. These disclosures are made through a private placement memorandum.

MASTER LEASES

An interesting feature of some TIC properties is the concept of a master lease. A master lease contractually obligates the sponsoring company to pay the rental income for a specific period of time as stated in the private placement memorandum. The master lease adds additional protection for the investor.

A key thought is the role that due diligence plays in the master lease. If the real estate sponsor makes a promise to pay the stated rental income, it is important to determine the real estate sponsor's ability to do so. Examining various financial statements and other financial information will help determine the sponsor's ability to back the master lease and whether this is a property that should be considered in the exchange.

A TIC may also potentially increase net cash flow to the investor because in many instances, property appreciation may outpace rental income increases. That's not a concern in most TICs. In addition to the potential appreciation of the TIC property, there may be substantial tax writeoffs, and there is no requirement for any time commitment by the investor.

As with any property, there are potential risks. The potential for property values decreasing, the loss of control, the potential for illiquidity and the potential for a reduction in rental income are all risks that need to be understood. Every investor has his or her own particular circumstances and should consider all options before deciding what is most appropriate for him or her. For the appropriate investor, a tenant-in-common program offers a viable option in a 1031 exchange.

David Fisher is a registered representative with and offers securities through AFA Financial Group LLC, a registered broker dealer, member FINRA/SIPC. Fisher Equity Advisors and AFA Financial Group LLC are not affiliated. Supervisory Office: 26637 W. Agoura Road, Calabasas, CA 91302, 818-708-0111. For more information, contact Fisher at 310-351-0373 or dfisher@fisherequity.com, *or visit* www.fisherequity.com.


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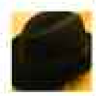
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