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What's a DST?

There's a new term in the investment world having to do with 1031 exchanges and that is a Delaware Statutory Trust or DST. Years ago you may have heard of a TIC or Tenants-in-Common ownership structure. That was commonly used for holding title to property with multiple investors. For the past 5-7 years the much more common form of holding title to a property with more than one investor is the DST.

A DST is a separate legal entity created as a trust under Delaware statutory law. This trust needs to be crafted in such a way as to satisfy the IRS requirements if it is to be used for a 1031 exchange (IRS Revenue Ruling 2004-86) and also it needs to be structured so as to satisfy any lending requirements in order to qualify for a loan. Fortunately, the Delaware laws regarding trusts are very flexible and will allow for all the specific provisions needed.

A few of the key components that need to be incorporated in the DST are:

- It is a Special Purpose Entity (SPE).
- It needs to be bankruptcy remote.
- It needs to be a passive holder of real estate, with minimal trustee powers over the operation of the DST's real estate.

Basically, the DST will hold 100% title to the property that has been identified by the "sponsor," the company that has purchased the property and will be the Trustee managing it. The loan (if there is one, the property could be debt free) will be a "non-recourse" note, which is held against the property only. One huge advantage of using the DST structure is the ability to acquire debt, which most investors need to satisfy the debt component on their downleg or property being sold. The investor in the DST doesn't need to qualify for these loans and the loan won't show up on the investor's credit report or financial statement. Most of the properties we've been involved with using the DST structure are in the 50% loan-to-value range, which is in line with most investor's needs. Again, these loans are non-recourse which means the lender can only foreclose and take possession of the property and the lender has no recourse for coming after the beneficiaries or investors as they are insulated from the lender coming after them by provisions in the loan and trust agreements.

On the other side of the coin, the DST structure protects the property and the other investors from any problems one of the investors may get him/herself into. For example if the investor, who is a beneficiary of the trust files bankruptcy or gets into a legal suit, the DST insulates the property and the fellow investors from those issues.

The trustee or sponsor of the DST will manage the property, keep all the accounting and issue statements, handle any leases, decide the best time to sell and basically run the show for this property

(and charge a fee). Many see this as a downside, since the investors have very little, if any, control. Obviously, it's important to deal with a sponsor that has a track record of being responsible and has enough experience to effectively deal with the many issues that can come up when owning and operating a property.

The DST structure allows multiple investors to own a single property and still qualify for a 1031 exchange. In addition, the DST can hold title to just about any type of property. Some of the DSTs that we've been involved with have held:

- Multi-Family Apartments
- NNN Lease Properties
- Storage Units Facilities
- Parking Structures
- Medical Office Buildings
- Assisted Living Facilities
- Office Buildings

One other advantage of the DST is that the minimum investment is usually \$100,000. This provides most investors selling an appreciated property with the ability to split their equity up into multiple properties and create a portfolio of different types of assets and also go into different markets across the U.S.

There are many more complex issues and provisions that you should be aware of if you are going to invest in one of the DST structures. This article is meant to give you a brief overview of them. For much more in-depth information feel free to log onto the links below for a wealth of excellent data concerning Delaware Statutory Trusts. As well, be sure and consult with your own personal tax and legal advisors, as each person's situation will have its own complex issues.

Louis Rogers: <https://www.youtube.com/watch?v=3Vo7NYdsynw>
<https://www.delawareinc.com/blog/101-on-delaware-statutory-trusts/>

For more information on DSTs, or for a personal, private consultation, give me a call at (626) 588-1520.

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