EPISODE 817

[INTRODUCTION]

[00:00:00] 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.

[INTERVIEW]

[0:00:23.9] WS: This is your daily Real Estate Syndication Show. I'm your host, Whitney Sewell. Today, our guest is Greg Lehrmann. Thanks for being on the show this morning, Greg.

[0:00:31.2] GL: Thank you, Whitney. It's my pleasure.

[0:00:34.2] WS: Greg is a double board-certified real estate attorney who has devoted his last 26 years to helping commercial real estate investors and brokers complete 1031 exchanges. He's here to show us the most positive surprises about 1031 exchanges. His information is absolutely critical to everyone in commercial real estate world and we're thrilled to have him on the show.

Greg, thank you again, welcome to the show. The 1031 exchange is a tool that everyone needs to have in their arsenal or in their toolbox. But it can seem very complicated and there's obviously timelines, everybody knows there's timelines, and they get worried about it. But I don't know that most have really looked into it to see how possible it could be for them to do it, or that it really the benefit. So, looking forward to the conversation, give us a little more about your 26 years helping commercial real estate investors and let's dive into your specialty, and just really helping those that are listening, understand some of the secrets about 1031 exchange and maybe even outlook for 2021.

[0:01:34.0] GL: Absolutely, yeah, I practiced law in the early ‘80s. And then I got the title business and I was running a bunch of closing offices. I had 85 employees in Dallas, Fort Worth, Texas. And then a couple realtors started coming to us and said, “Greg, why don't you all do 1031 exchanges? We have investors that sell real estate without paying taxes, totally legal under the tax code.” And I thought, “Well, I've got an accounting degree and a law degree. Why don't I know what that is?” It turns out, it's a niche. It's a real niche. There are very few people in the whole country who really specialized in this area to this day, even though they've been around now almost 100 years.

The blessing of those realtors bringing it up is it taught me it's a real thing. And it taught me to keep my eyes open for any chance to start doing it. And so, in 1993, the company that I was president for in Fort Worth, Stewart Title Nationwide, announced they bought one of the two biggest 1031 companies in the nation called Asset Preservation, Inc. And man, I hit the ceiling with excitement. By October of ‘94, I went from the closing in to the 1031 in and haven't looked back. So, I spent 100% of my time, for the last 26 years doing two things. We do all the work that someone needs for a 1031. So, we provide that direct service.

What we also do is we educate the public, because there's so many opportunities out there for people to save their money and build wealth a lot quicker and bigger by knowing about 1031. So, it's still a blast after all these years to me to share this information. They learn what people need to know about it and how much they can learn in one 30-minute segment.

[0:03:17.9] WS: Yeah, that's awesome. So yeah, let's jump right in, because you are definitely an expert in this field. And I want to pull some of those secrets out, from you that you know about that our listeners need to know. And obviously, most of listeners are passive investors who are trying to invest in syndications, maybe they have small rentals that they're exiting. I get that call, often, more and more often, investors saying, “I've been in real estate for 20 years and been managing it, and now I'm trying to sell my stuff and just go completely passive. Whitney, can you help me? Can I 1031 into one of your deals?” So, that's a very common thing. And then there are guys who maybe owns some smaller properties and want a 1031 into something larger, and they're trying to get into this business as a syndication or even a passive investor syndicating from one deal to the next — and just love your opinion on even as an operator, how we can do that and help that investor.

So, get us started, I guess, are there some secrets that we need to think about right off the bat, that we need to know about 1031 exchanges that maybe there's some myths or anything like that?

[0:04:21.4] GL: Absolutely. Even though there are a lot of issues for us to know about, because we're the ones that handle it. We thought of about 180 issues that we've written papers on, that can come up, but that's our job, and the job of the person's tax advisor to collaborate with us to dig deep into those. But what people need to know, what the investor just needs to know is three words. It is just three words. I thought this was so complicated before I dove into it and I found out. It's just three words, it's like, kind, and it is exchange, and it is Qualified Intermediary. None of those words mean what they say. So, you have to start with a fresh, open mind when you're hearing these words with 1031s. The term like, kind, and exchange are about a million times better than they sound. So, when you learn those words, it opens up a lot of opportunity.

And then the word Qualified Intermediary is actually a lot worse than it sounds. So, if you don't learn what that means, you lose everything you thought you were about to gain. So, we can dive into like-kind and how much better that is than it sounds. Although of course, with anything, there's still some limitations, especially when it applies to syndications, but every investor needs to know enough about 1031s to know to check them out and call somebody like me, or somebody else they know in my position, the trusted expert, they know that really knows those 1031s. And I've really got to basically recommend to 1031 people who pretty much do this full time. There are people who do this on the side. And if you've got a great person that does that, that's fine.

But generally, you need somebody that best knows 1031. So, like and kind, why is it so much better? Why do I say it's so much better than it sounds? That is because what an investor gets to do, if they're selling something, all I got to ask is, is it in the United States and is it a real property interest that they were holding for use in their business or for investment? So, if you own a business, and you own the real estate, and you want to get out of that business — when you sell that real estate, you don't have to pay any taxes. If you buy other real estate that qualifies, well, guess what qualifies, it has nothing to do with what you sold. That's why I say like kind is a misnomer and it's so much better. You get to start over, you get to buy anything in the

United States, that's a real property interest, that you're either going to run a business out of, or hold for investment.

So, I had someone sell a restaurant in Florida, and they owned the land and the buildings, and they did a 1031 into some real properties in Texas. And see that's absolutely like-kind. So, the category of like - kind is really broad.

Let me even back up and simplify this even more to give everyone a complete understanding of why this is in the code. And that really simplifies it and makes it understandable. In 1921, farmers went to Congress and said, “Look, if we've been in farming several years, and we've built up equity, and we can trade that farm for a bigger farm, that's going to be better for our family. And guess what, it's going to be better for the economy and that's better for the US Treasury.

But if you are going to tax us on going from a farm to a farm, and you show me how the heck I can pay taxes with dirt. That's all this means.” And Congress saw that basic elementary wisdom 99 years ago, they said, “Oh yeah, if we tax people, when they're going from dirt to dirt, they can't go to that dirt, and we're not going to get their tax money anyway, if we let them trade up, without paying taxes, they can do that. And then Home Depot makes more money, the gardeners make more money, the real estate agents make more money, the title companies make more money, everybody makes more money. And then they pay more taxes to the government that they come out ahead, the people do, because they still make more money, even after taxes off their income.” And then the US Treasury gets their money that way. It helps GDP, it helps jobs.

So, that's all this is. It makes so much common sense. But then over the years, the definition of like and kind has been expanded as broadly as I just mentioned. One person who's done these many years, he said, “Greg, just tell people like-kind means, if they like it, kind buy it.” So, it is very broad. It's a big enough surprise for even some CPAs that you can sell a bunch of single-family rental properties and buy an apartment complex. But you can even sell residential investment and buy commercial. You can sell in one state and buy in another state. You can't buy it in another country. It’s just US. You don't even have to be a US citizen, you qualify their property. So, you're just selling business or investment real estate that you bought to hold. So it's very, very broad.

[0:09:18.3] WS: What about the exchange word?

[0:09:20.3] GL: Exchange doesn't mean exchange. From 1921 to 1991, exchange meant exchange. They limited these to when like you and I trade. So, Whitney, if you wanted my property, the only way I could sell it to you without paying taxes is if it just so happens, you have something I want, or about the most creative thing that you could do before ’91, is I would find what I want and I would have to convince you to buy what I want. And then we would do a swap. So, exchange used to mean a direct swap. And in ’91, real estate investors went to Congress and said, “Look, that's crazy to do it that way. Just let us do more like a roll over like a retirement account rollover.” That's another way to simplify this. This is similar to a retirement account rollover, but you can do it at any age. And there's no time when you have to start paying taxes as long as you're in real estate.

So, they went to Congress, and they changed the law in ‘91. And they said, Congress said, “Okay, just sell to whoever wants your property so you can take as good of an offer, as you would have taken before. You're not limiting your buyers to those that want to get involved with you, just sell, take your best offer, and as long as you have another company, hold your money between the sale and the purchase, we're not going to tax you. And we're going to give you 180 days between closing.” So, that's how much they expanded it from having to do a direct simultaneous swap. But they also said you do have to identify the property within 45 days after you close.

So, the timeline is, first of all, you cannot do a 1031 if you don't have documents at the closing of your sale, but that can be so easy if you deal with someone who only focuses on this. Since this is all we do. We have literally had people call us from the closing table that we've never heard of before. And they say they want to do a 1031, we need to have one conversation with them to make sure they understand all the fundamentals. We need the contract and the title work, and from that, we do exchange documents and we email it to the closing. We've done that in less than an hour before. I don't promote doing it that way, but you have to have documents at the sale. And as long as you have that, now you have 45 days to identify a group of properties and we can get into the weeds on the different ways of doing that. But the big picture is, you've got to put together a list of properties you're considering within 45 days, and they give you a full 180 to close.

The 180 is almost never the challenge. The common challenge, as you know, I'm sure Whitney, is identifying within 45 days. So, when I first heard about 1031s, I got very excited. And then I found that you got to identify within 45 days, I got deflated. I thought, “Oh wow, that's hard.” I figured out, “Look, the smart investors who learned about this, they don't wait till they close their sale to tie up a property.” So, you have unlimited time between now and the closing of the sale, and then another 45 days to put your list together. And the main way that you can do it, there are other ways, but the three-property rule is the most common.

So, let's say you just want one property, the three-property rule allows you to list three properties. And you can switch those out during the first 45 days, but not after that. But if you listed three properties, and you got past day 45, then your number one choice fell through at least you have two more on your list. But you can't go grab another one somewhere else. But you can just go down your list and then close within 180. So, exchange ever since ‘91 hasn't really mapped the exchange the way you think of Whitney and I having to swap with each other. You just sell with the right kind of documents, you identify what you want to buy within 45 days and close within 180. And then the company that's holding your funds, sends the money from your sale to the purchase. And it's over with so many people say, “Oh, wow, I barely noticed anything was different.” So, that’s where the exchange is.

[0:13:27.8] WS: Okay, let's jump into the Qualified Intermediary. And then I want us to move into a couple other things.

[0:13:33.9] GL: There's good news and bad news with Qualified Intermediary. So, I mentioned the good news is when they came up with this way to just sell and buy, oh, that was wonderful. And they said, “Oh, just have your money held by a Qualified Intermediary and we won't tax you.” The problem is the definition of Qualified Intermediary. There are no qualifications. So, that also doesn't mean when it says, Qualified Intermediary does not mean that the person is qualified. The actual definition of the tax code is a Qualified Intermediary is anybody in the universe who is not disqualified. And guess what? They don't disqualify people who are in prison today for embezzling other people's money. Nobody is disqualified except the person's relatives or their agents. It only means someone that's independent. Congress said if you're not going to pay taxes, you have to have your money held by someone outside of your control up to those 180 days. That's literally all it means.

So, they don't disqualify people who have never opened the tax code or never done a 1031 or have stolen other people's money. So, that is the bad news. The good news is it's so easy for a prudent investor to deal with that. Because even though qualified intermediaries are not automatically regulated, there's no regulations per se, of all qualified intermediaries, the way most prudent investors protect themselves, is they just go hire a Qualified Intermediary that's owned by someone who is regulated. So, just because QIs are not regulated, it doesn't mean you can't find a QI that's owned by a regulated company. So, that's why Stuart Title bought this company. And full disclosure, all the major title companies have major qualified intermediaries that know what they're doing and we're one of them. So, that's the way most people deal with that.

[0:15:33.9] WS: What's a couple of quick questions that say the investor could ask to know that they're dealing with somebody reputable?

[0:15:41.1] GL: Yeah, who backs them? Who owns them? And does the entity that owns them do a direct guarantee, like Stuart Title puts their name behind our handling of the 1031s, and if one of our employees figures out how to embezzle the funds, the investor has Stewart Title on the hook, just like they rely on them every day to ensure properties. So, you want to ask who guarantees the performance of the QI? Do they put it in writing where the money goes? Because there's not even a rule that says the money goes in a bank. So, there are QIs that weren't crooked, some have been crooked and stolen the money. Others weren't crooked, but they put the money in like a stock that went bad. And so, the money's gone. We of course, put in writing that we only put the money in the bank.

Another thing is in whose name is the account. There's not a rule that says the investors name is not even on the account. So, the way some QIs have been able to use the money is they – the QI just put the money in the QI's name so we put in writing, each person has their own account, and their name is on their account, along with ours. Ours has to be on the account.

Otherwise, it's taxable. So, we have to be one of the people that the bank has to go to to authorize transfer of funds. But we do it to where the investor has to authorize also.

And then when it requires our signature, it requires multiple people in our company to authorize the transfer. Therefore, you don't have the situation where one person is in control. Really, the embezzlements that I'm aware of, it's been one person signing the checks, being in charge of reconciling the bank account. All that, as you probably know, Whitney, somebody like us, a big company –

[0:17:29.4] WS: Right, no doubt about it. There's no accounting of the employees or whoever's in charge of it. Greg, let's jump into quickly just the outlook you see for 2021 concerning the 1031 exchange. Let's dive in.

[0:17:41.0] GL: The outlook is well, I've got an email saying, "Okay, I heard 1031s are going away." Well, and that is because initially it was in Joe Biden's – it's been in his plan for a long time, that he was going to look at eliminating 1031s as a way of paying for all these stimulus checks that had been written and all that. But there's really no reason to freak out. Because believe me, that proposal has come up for 99 years. And so, we just constantly have to go to Congress and explain 1031s again, and how much it would hurt GDP and job creation, if you took it away. And that's the last thing any Congress wants to do is kill GDP and kill jobs. So, it just takes reeducation. The initial proposal has already been modified to just do away with 1031s over pretty high-income levels.

So, the outlook is we've been working on this already for a year, educating the people who might get elected and who are just getting reelected, to stay in touch with them. We stay in touch with them, the whole industry does. It's not just the QI industry. There are so many industries that would be harmed. So, they're always involved. Anybody involved with real estate, National Association of Realtors, Builders Association, tons of them are always involved in educating. So, the outlook is just that we need everyone talking to any elected official that they know — explaining how much of their livelihood depends on the real estate industry and how much the real estate industry relies on 1031. Every year, 35% of all land sales are 1031s.

So, that's the outlook is just that we all need to actually keep 1031s in play. Right now, they're going gangbusters. So, many people are surprised in this economy. We're doing as many 1031s as we did pre COVID. Early in COVID, we only had about a six-week, about a 40% drop in 1031s for a while and then people readjusted and there's all this pent-up demand. So, if 1031s are going wild, because more and more people learn about them and what it does for people, you can preserve your wealth. You can deal in real estate your whole life and never pay taxes which is unbelievable. You can leverage up. Let's say you just have 30 grand in taxes you would have paid. If you're putting 25% down in the next property, 30 grand that you'd defer as 120 grand to what you can buy, that's just on a regular smaller residential deal. So, that's kind of the outlook is very strong.

[0:20:21.1] WS: Can you speak to the passive investor that's listening right now? Or let's say, the investor who has some small multifamily and they call me and say, "Whitney, I'm ready to retire from managing these properties, I want to sell them. It is possible for me to 1031 into your syndication?" What do they need to know? We don't have a lot of time left, unfortunately. Or maybe we'll have to have you back to dive in a little more. But what are some things they need to know as a passive investor, and then even as the operator listening, what are a couple things they need to know?

[0:20:52.4] GL: Yeah, a huge pleasant surprise to people is that you can sell very high maintenance real estate and buy 0% management property. You can either buy your own triple net leased property like a Walgreens, or you can buy a percentage in oil and gas wells. And then the third one, which is not third in priority, is probably the most popular advice when they get to your point at the end, is that you can buy a fractional interest in a piece of real estate. So, the great news is, you can buy a one-millionth of 1% interest in a piece of real estate and that qualifies. The only challenge is, despite how broad the category of like-kind is, it is still limited to direct interest in real estate. So, it just has to be set up as a tenancy in common, instead of a limited partnership. A partnership interest does not qualify, but a tenancy in common interest does qualify.

So, those are the options for passive investors and that's going more and more. The biggest trends with 1031s is people getting out of high maintenance, real estate, but they don't want to give their gains to Uncle Sam, and they have learned that they can buy low maintenance, real estate through syndication, as long as they basically are on the deed, even if it's a one thousandth of 1% that does qualify if it's a direct interest, so that's how they do it. It’s amazing.

[0:22:11.6]WS: As the operator, how much should we expect that investor to be bringing to make it worth their while, and there's quite a bit of expense, for us to do that, to create the tenant in common structure. And some of those things are legal expense. So, I've heard different operators say, what that investor has to be bringing at least a half a million or a million or, things like that. Did you have a figure like that you've seen a lot of people use and say, “You know, what, if you're only only bringing $100,000, it's just really not worth the trouble.” Or what have you seen?

[0:22:41.0] GL: Well, it depends on how the operator is set up. There are things called DSTs, Delaware Statutory Trust, where some major players have set up DSTs. And I think it's a very expensive, I think, to get started in that. And then I think they're able to do it pretty efficiently. Because I've heard some of the larger operators will take as little as 100,000. So, it just depends on what all is involved in setting up that deal for that particular project. So, yeah, it works out as little as 100 grand for some people that have already joined this deal up, if it's your first deal setting up. Yeah, imagine half a million is what pencils out a little bit better and worth the time. So, yeah, depends on what kind of sponsor you are.

[0:23:30.2] WS: Sure, Greg, just a few final quick questions. What do you expect to happen, in the next, say, 6 to 12 months in the real estate market?

[0:23:38.6] GL: Well, again, there's been pent-up demand, we're doing as many 1031s, like I said, as ever, the types of properties have changed, we've done more residential, residential investments are going crazy. More people are buying properties outside of town — you can actually buy a vacation home, if you do that right, and eventually retire there. So, more people are buying outside. Farms and ranches are still just so popular. And it's more residential and in the commercial arena, of course, it's no surprise. More industrial warehouses, Amazon warehouses, things like that, and not so much, downtown office space.

So, yeah, we'll see. But it still looks like it's going to be a strong real estate market, even though some people are benefiting more than others, depending on the property type that you own.

[0:24:31.3] WS: Greg, do you have a couple of daily habits that you are disciplined about that have helped you achieve success?

[0:24:37.1] GL: First, I'm so into educating people that each morning before I think about, “Okay, who can I educate today?” Because that's how we build our pipeline. I have to focus on my current customers, because I go back and forth between educating people and actually counseling people on pending transactions. So, I always have to start out making sure, and then that falls through the cracks. Finally, after many years, I've put a bulletin board on my wall in my house, like you see in companies and how they keep track of their deals going on. So, my daily practice, really, it's not really personal, it’s just business. But it's first making sure I'm taking care of current customers and what's the next step to helping something get to the closing of their 1031. And then I get to thinking about, “Well, who else needs to know about that.” And setting up more Zoom talks. So, I do Zoom talks, once or twice a day, practically, to realtors and investors and CPAs and attorneys. So, that's basically what I do.

[0:25:41.7] WS: What's the number one thing that's contributed to your success?

[0:25:44.4] GL: Just following the latest trends, being open to learning new things. I've been around a while. So, to be honest, several months ago, I got into the Grant Cardone system. And that opened my eyes to a lot of things. He's one of the number one sale’s trainers and met a lot of people through that who are entrepreneurs that build their business. So, it's sticking to one thing that I know, so that I know I can give great answers with a phone call no matter where I am, but also learning the new ways to stay in touch with people. That's been really, really exciting, like doing podcasts like this. It's a good example.

[0:26:26.2] WS: How do you like to give back, Greg?

[0:26:28.1] GL: Wow, all kinds of ways. Generally, I have friends, it's a little bit indirect. Well, I'm a member of a rotary club. And we have, of course, a lot of projects, I participate on those. And then I'm constantly seeing that my other friends are involved in something and they say, “Hey, we need help here.” Usually, a financial. If someone asks for a donation. Why donate? I see that, “Well, that's good.” So, it's a little here, a little there. It's very broad based, I just support good causes. And since it's so many, it's just, “Okay, I'll do a little here, little there. It may not big for this person, but a little bit here a little bit there, all adds up.” That’s the way I give back.

[0:27:10.0] WS: Sure, it does. Well, Greg, I'm grateful for your time today and just really getting to meet you knowing that you’ve been in the 1031 business for these many years and just an expert. It's great to know you personally. And I hope the listeners will also remember you as they are considering making that exchange, doing it legally, and with somebody that's qualified, for sure. So, just grateful for you just breaking down those three words. And then just giving us your outlook for 2021. I think that will help calm some people's nerves a little bit, about the potential of doing their 1031 next year sometime or the year after, even.

So, Greg, how can people get in touch with you and learn more about you?

[0:27:46.3] GL: So, my number comes right to my cell phone, (866) 266-1031. Email is greg@apiexchange.com. It's API for Asset Preservation Inc. So, greg@apiexchange.com and I'm on Instagram, @greglehrmann1031. So, yeah, please get in touch. That's what you need to know, really, you need a phone number. The way to do 1031s to wrap this all up, is to have the phone number and email address of someone who focuses on this exclusively and has done it a long time. So, that's all you need to remember about 1031s is how to find a good resource. And I would like to be that for you.

[0:28:34.9] WS: Awesome, Greg. That's a wrap. Thank you very much.

[0:28:37.4] GL: Thank you.

[END OF INTERVIEW]

[0:28:39.6] WS: Don’t go yet, thank you for listening to today’s episode. I would love it if you would go to iTunes right now and leave a rating and written review. I want to hear your feedback. It makes a big difference in getting the podcast out there. You can also go to the Real Estate Syndication Show on Facebook so you can connect with me and we can also receive feedback and your questions there that you want me to answer on the show.

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[OUTRO]

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