How to Retire while Your Real Estate Capital Keeps on Working

last of a four part series

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How does a wealthy household receive safe and solid cash flow, eliminate management stress and preserve capital for the next generation? They *exchange into safety*.

Thousands of successful investors have used this strategy to succeed. This article crystalizes their wisdom. It is the last of a four-part series about legacy wealth. The three previous articles described some ways to build wealth safely: rehabilitation, repositioning, and sheltering income from taxes with classic properties. Those articles are available at **www.sddt.com**

Part Four: Exchange Into Safety — "Preserve My Wealth and Provide Steady Income"

Chuck and Betty Johnson are contented grandparents. They became financially independent through investment real estate. They are ready to enjoy more cash flow and are done with toilets and tenants. They are patriots, but they won't pay taxes early or pay more than their fair share.

On a teacher's salary and one other job, their income was never large. But the Johnsons saved and then invested prudently. They helped their kids with college. Now social security, a modest pension, and rental income cover their expenses.

Challenge:

Last year their rental property was worth $2 million and was nearly paid off. If they had simply sold the apartments the income tax bill would have been $750k+, which they found excessive. Their 45-yearold building was getting older and so were they. Maintenance hassles were becoming big chores. When they didn't do the work, they found the charges for maintenance to be astounding.

They love their adult offspring, but those adult kids didn't have 50 years of investment savvy. The Johnsons made this next solid choice before the risk of Alzheimer's, stroke, or some other major issue.

What is more appropriate at this life stage?

Time is precious. Grandchildren, friends, hobbies, and travel matter. Doing physical labor, trying to meet tenant expectations or working just to build a bigger estate is not worth it. More cash flow, low risk cash flow and security of capital are more important than chasing more appreciation. For the Johnsons, more and steady cash flow without property management is appropriate.

What solution did Johnsons select?

They sold their $2 million, older apartment building and used a tax-deferred, "1031" exchange. Section 1031 is IRS code for tax-deferred exchanges. A 1031 enables people to maintain their wealth and move their equity into another investment.

They bought a newer $3 million commercial asset with a long lease, rented by a national firm with net worth far larger than their own (we'll call it an NNN or triple net building). The new loan, prudently about 50% of the value, was $1 million more than the balance on their apartment loan. The extra depreciation and interest deduction shelter about $70,000 of annual income.

They were pleasantly surprised to discover that the NNN provides better cash flow than their apartments. Their cash flow increased, both before and after income taxes.

According to actuarial table the loan will be retired before the property passes to their heirs.

What is a single tenant, triple net building?

Single tenant means there is only one business in the building. Triple net describes the payment the investor receives. The rent check is net of tax, net of insurance, and net of all other property expenses. The corporate tenant pays for all the costs and landlord has a simpler life.

What kind of the tenants rent NNN buildings?

Look at free standing retail buildings, occupied by national firms. Tenants include: banks, convenience stores, national sit down restaurants, fast food places, office supply chains, automotive parts retailers, drug stores and, dollar stores. FedEx and other national firms rent warehouses that are sold as NNN. Although there are some small local shops in free standing buildings, their credit is not appropriate for retired investors.

Why do so many mature investors buy NNN?

Mature investors seek steady income with minimal risk. They insist on strong credit and leases of at least ten years. Most NNN properties have rent increases, often 10% every five years.

The Johnsons have seen inflation boost their net worth. "We would rather have inflation work on more property instead of less property."

What risks are involved?

Every investment, even 30- year T bills, have some risk. Many mature investors prefer an NNN because even if some life altering event occurs like Alzheimer's or stroke, the income is always there. NNNs have lower vacancy than any other property type. For example, 99.5% occupancy for an NNN is safer than 95% apartment occupancy or 80% office occupancy.

The investor selects which level of return is best. by weighing the credit risk. Safer investments have lower returns and vice versa.

Application

Mature investors who want steady income, with no management and low risk should consider trading into NNN properties. A CPA, trust attorney, or other trusted advisor can assist families in making a wise choice to produce the best possible result.

Terry Moore, CCIM, principal of **ACI Apartments**, has helped nearly 400 households build and transfer legacy wealth. His calling is to help families make wise choices about their income property wealth. He has completed nearly 50 tax-deferred exchanges and sales of income property for estates. He was recently recognized as a "Top Influential" by *San Diego Daily Transcript*. Reach him at **TMoore1031@gmail**, **619-889-1031** or through **SanDiegoApartmentBroker.com.**