The Tax Litigator's Detailed Guide to Tax-Free IRA, HSA and CESA Wealth

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HOW TO USE THIS COURSE

This course consists of both written and audio material. If you neglect either, you shall have deprived yourself of a great deal of valuable knowledge. The audio portion of the course consists of approximately 14 hours recorded on August 22 -23 2015. The recording is of a 2 day workshop I presented called "IRA Meets the NRA". The title comes from the fact that the workshop was at a five-star shooting range. After the classes, we went shooting, which was of course tax-deductible entertainment, including some incidental supplies. There were approximately 20 attendees. Most of them were highly experienced and creative people. Indeed, the constant and excellent questions they asked both reflect their experience and should provide you with a great deal of food for thought. The audio is segmented into relevant topic areas, so you need not listen to all of it consecutively. Also, many of you purchased access to one of the two-day IRA workshops I host two or three times per year. Listening to the audio and reading through the course should give rise to a number of questions. I look forward to discussing those question at a workshop, in an advisor-client relationship, or both.

<u>THE TOP TEN CONCEPTS I HOPE YOU ABSORB AND ACT UPON</u>

1) Most people, including for experienced and savvy investors, underestimate just how much an IRA can save in taxes. Most readers of this publication should be able to save millions in taxes by applying the principles herein. That statement is neither puffery nor exaggeration. Focus on the very examples on pages 9-13 and in sections 12 and 13 of the audio for proof of what I am saying.

2) A thorough understanding of the prohibited transaction rules is essential. One tiny prohibited transaction will quite literally destroy an IRA. Both written and audio materials spend a great deal of time discussing those rules. That allocation of time is not accidental. Please prioritize accordingly.

3) Traditional IRA's are very powerful. Roth IRA's are much more so. The difference in the power of each account type is the difference between "tax-deferred" and "tax-free". For most of you, the latter is a much better option.

4) For most of you, a 401(k) or Solo 401(k) beats an IRA – and you can actually have both. IRA's are powerful tools, easily able to save normal investors seven-figure sums. 401(k)'s represent a quantum increase in power over IRA's. The savings to be had via a Roth Solo 401(k) are especially impressive. In one cannot save seven sums of taxes with a mere Roth Solo 401(k).....then one is doing something wrong.

5) Small accounts can grow into very large accounts. Do not ignore the power of leverage. I know of an investor with over fifty free & clear rental properties in a Roth IRA. He is over 60. Meaning: The rental income of 50 free & clear rentals comes to him monthly – *tax-free*. Not

tax-deferred. *Tax free*. He did it through the intelligent use of debt. You will read more about his example later on.

6) Understand UBIT. UBIT is a tax on otherwise tax-deferred or tax-free accounts. Understanding it allows one to avoid – or to intentionally pay it when the returns are 20x or greater than the tax paid.

7) Please Do not neglect health-savings accounts ("HSA's"). They can save massive sums on healthcare, now and in the future. Worst case, they can allow for additional tax-free growth and defer income taxes until you pass away. I have used mine to escape the increasingly socialistic and inferior US healthcare system by using overseas healthcare, aka "medical tourism". My carefully-chosen overseas doctors cost me a fraction of my US doctors – and exclude bureaucrats, lawyers and insurance companies from our relationship. Almost everything that can be done in a self-directed IRA can be done in an HAS including massive tax-free growth of your investments.

8) Please do not neglect Coverdale Educational Savings Accounts ("CESA's"). **They can fund private schooling K-12 and a college education – tax-free.** They can also fund personal computers, printers, other equipment and supplies, internet bills & other utilities for an *entire* family – tax-free. Similar to HSA's, CESA's can do pretty much anything a SDIRA can.

9) Please do not use so-called "Checkbook LLC's" without being fully informed as to when they are useful and when they are not. Likewise, if such an LLC makes sense for you, be sure that it is created and run correctly. Most of the CBLLC's I have seen are drafted by people (including lawyers) with no clue about IRA law. They are a disaster waiting to happen. For example, CBLLC's that allow an IRA owner to manage the LLC are as common as they are deeply flawed, because such self-management may constitute an IRA-destroying prohibited transaction.

10) Unlike most course authors, I am not a mere theorist. I am an attorney, accountant and real estate investor. Very few attorneys or CPA's understand this area of the law. Fewer still have audit experience in this area. And while I am sure they exist, I have never met any attorneys who have successfully defended self-directed IRA in Tax Court. I have done all of these things, which provides me with a nearly unique insight into both the possibilities and pitfalls of SDIRA's. I mean to share that experience here.

Here's to you keeping more of your hard-earned dollars!

BASICS

What is an IRA?

An IRA is a trust. As is the case with all trusts, the trust itself is owned and managed by a trustee. The trustee is normally a trust company. IRA trust companies come in two basic flavors: Custodians and third-party administrators ("TPA's"). For our purposes, the terms trustee, custodian and TPA are pretty much interchangeable. I will normally use the term custodian.

The person who contributes money to the trust and who can ultimately pull tax-deferred or tax-free money from it is the "account owner", "IRA owner" or "owner".

The IRA beneficiary is the person who stands to inherit the IRA if the IRA owner passes on.

What distinguishes an IRA from a regular trust is a special set of IRS rules that allow the trust to defer taxes, or to avoid them altogether.

Basically, you put money from your job or business into an IRA. You may or may not get a tax deduction for having done so. The money then grows tax free. When you are old enough (generally but not always 59.5 years old), you can take money out of the IRA. Such distributions may or may not be taxable.

Who Cares?

IRA's can defer or even **eliminate** millions of dollars in taxes.

Millions.

Further that number easily applies to the **average** investor. If you operate above the financial average, then the tax savings could be in the eight figures, as they were for failed presidential contender Mitt Romney. More on "how" such savings occur in a minute.

How are most IRA's invested?

The vast majority of IRA's are simply invested in Wall Street. It's easy to simply Wall Street your money. They direct the investment, you pay them to do so. For most people.....that's probably not working out very well. Here's why:

- Socialism is expensive. In order to pay for at least some of the promises it has made,[1] both the US and most state governments have borrowed far more than they can ever repay. For the last 2,000+ years what do governments that cannot pay their debts do? They debase their currencies.[2] One way to do that is to create more money and to artificially lower interest rates. Almost every government in the world is doing exactly that. Which is why many portfolios are

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[1] That healthcare wasn't free. Duh.

[2] For an outstanding, thoughtful and detailed discussion of this historical **fact**, I recommend *This Time is Different*, by Carmen M. Rinehart and Kenneth Rogoff.

returning 1% or less in income – the government has artificially suppressed interest rates. Bottom line: Socialism encourages governments to rob from savers who did the right thing their entire lives. One way that governments accomplish theft on such a grand scale is to drive down interest rates. Those very low rates mean that many Wall Street instruments provide tiny returns (but it also means that the governments' massive debts are easier for them to bear). Taking inflation into account, many debt instruments actually provide negative returns – meaning savers are actually paying Wall Street for the privilege of holding their money. Madness.

- Wall Street does not pass the good deals on to normal investors. Most WS instruments have a number of analysts following them. That means that competition for yield is fierce and bargains are hard to find. When an analyst finds one of those rare bargains, he will likely profit from it directly and share the remainder with his favored "insider" clients. The investing public generally does not have access to such deals. Indeed, securities laws designed to "help" the public often make passing good deals to that same public risky for Wall Street promoters.[3]

- Wall Street is not very trustworthy. We all know that Wall Street sold lousy deals to lots of people during the boom. They certainly made their money, even if the investors lost theirs. And that money has been well invested in politicians. Barack Obama, to name but one example, raised record amounts from those people. It is surely a coincidence that not only was there no penalty for Wall Street's behavior, they were actually rewarded for it in the form of bailouts. In fairness, Wall Street's activities were desired by and encouraged by politicians on both sides of the aisle. In such an environment, Wall Street has little incentive to be very honest.

- Wall Street does not share primary information with public investors. Wall Street sees a lot. They filter that information for the public. That information is often "less than accurate", to put it politely. Remember Arthur Andersen and Enron? In fairness, the information that Wall Street provides us is *far* more accurate than what the government reports on its income statements and balance sheets.

- Wall Street undermines the economy. Wall Street causes otherwise good companies to mis-invest to "show better numbers" in order to generate immediate windfalls for itself. The costs in terms of actual productivity are immense. For an excellent discussion from a very credible source[4] on exactly how this occurs, take a look at: http://www.mauldineconomics.com/outsidethebox. Search for the October 28, 2015 article entitled "The Financialization of the Economy". Mauldin has a number of other publications. I have found that they – and the publications/authors they recommend – are simply first class.

Bottom line, you are likely better off investing in what you know than you are in trusting Wall Street.

What's a Self-Directed IRA?

Instead of trusting Wall Street to invest for you, you direct what your IRA's investments. You decide whether to invest in rentals, rehab & retail properties, loans, small & private companies, gold, silver,

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[3] For example, "accredited investors" with a high income or asset level have access to deals that are not made available to the general public.

[4] No black helicopters.

livestock, etc. You can invest the IRA in almost anything. The only investments that are *directly* prohibited are:

- No life insurance
- Certain types of derivatives
- Antiques and collectibles, which include but are not limited to
  - stamps
  - Most coins
  - furniture
  - porcelain
  - antique silverware
  - baseball cards
  - comics
  - works of art
  - gems and jewelry
  - alcohol
  - Any rugs[5]
  - electric trains and other toys
  - certain types of coins and precious metals, with some very liberal exceptions

Certain other investments are *indirectly* prohibited (e.g. – a loan to yourself or to most family members). Such prohibitions arise from the operation of the complex "Prohibited Transaction" rules found in Internal Revenue Code Section 4975. We shall spend a great deal of time exploring those rules later in this publication.

Like political liberty, SDIRA's reflect upon the underlying humans who are making certain choices. It's not a coincidence that under the aegis of freedom, the most prosperous civilizations in the history of our race have grown and brought longer life and greater comfort to all. But abuse or neglect your liberty, and you will lose it.[6] Likewise, a SDIRA allows you to make massive returns, certainly far in excess of the norm....if you do the *right* things. But it also allows you to lose *everything*, especially if you are sloppy or ill disciplined. True self-direction, like true liberty, means opportunity in two directions – up *and* down. Just remember: Your custodian's job is to act as trustee to your IRA, which is a trust. It is NOT your custodian's job to provide tax or legal advice, to keep you from entering into bad deals, or to keep you from engaging in prohibited transactions. That is *your* job. If you are the sort of person who does not behave responsibly or who likes to blame his own problems on others – then a SDIRA will be an absolute disaster for you.

Bottom line: SDIRA's can fund a great many unconventional investments – as long as the rules are followed.

<u>If SDIRA's are so great, why aren't they better known?</u>

Most people are "too busy", too incurious, too limited in their thinking, too lazy or quite simply too stupid to pay attention. Or to follow through. The government of course loves such people – *they* pay far more than they must to fund an ever expanding and increasingly harmful bureaucracy. The fact that

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[5] Presumably does not include carpeting for your rentals.

[6] Which is exactly what we are doing. Those who prove unfit to rule themselves shall be ruled by others.

you are reading this material likely means you do not belong in the unflattering categories I described above. Of course, for any knowledge to be of use, one must **follow through** and transform abstract thoughts into concrete reality. **One must act.** I mean to show you how to do exactly that. It is my hope that you shall exert the discipline and effort needed to kindle the spark that is this publication into a lucrative reality. Starve the bureaucracy – they deserve it. Keep the money, *you* earned it. You *did* build that.

OK, how exactly can an IRA save ME millions of dollars in taxes?

To answer that question, I shall start with a grossly simplified explanation. For most readers, that explanation will not suffice to truly bring home the point. Which is why I have included several examples that are worth taking the time to read through. If those examples fail to persuade you....then you are beyond my power to reach.

The Grossly Simplified Explanation

"Traditional" IRA's invest on a tax-deferred basis. You contribute money to them and get a tax deduction, normally equal to the amount contributed. More importantly, the income generated inside the account grows tax-free. I cannot over-emphasize the importance of this feature, you will see more on this in a few paragraphs. Once you withdraw the money, it is taxable. For a Traditional IRA, the tax savings come in three forms:

1) The tax deduction normally received on the amount contributed to the IRA;

2) The ability of the investment in the IRA to grow tax free

3) The deferral of taxation until you start withdrawing money from the account.

Roth IRA's function differently than Traditional IRA's. Both Traditional IRA's and Roth IRA's allow for tax-free growth of funds held within the account. Where Roth's differ from Traditional IRA's:

1) Contributions to Roth IRA's are not tax deductible; and
2) Money withdrawn from Roth's is withdrawn tax-free.

For most people, the comparative upside of Roth IRA's (money can be withdrawn tax-free) **greatly** outweighs the downside (contributions are not deductible for tax purposes).

But the idea that one grow money in an IRA tax-free and distribute it from a Roth tax-free is so *abstract*. Many people "know" this, without truly understanding what it means. I find it easier to communicate the **vast** amount of taxes one can legally dodge with examples and numbers.

Four Examples That Make the Case

Nothing makes this point like numbers. Please examine these examples. Take your time. Analyze them. Question them. Check my math. Most of all – *understand*. An immense amount of useful data lurks in these examples.

For the first example, let's assume that you start with $100,000 and do just one buy-rehab-sell deal per year that returns a 30% profit. For simplicity's sake, I am assuming that the entire cash balance is invested in the flip. Let's set the tax rate at 35% for combined federal income, state income and social security/self-employment taxes.

At the end of ten years, your cash balance if you paid taxes would be $593,893. If you did not pay taxes, the cash balance would be $1,378,525. **Due to the tax you paid and the compounding that you lost, the government robbed you of $784,732.** Lest you doubt my math, I have included it in the chart below. Take your time, go through it line by line. Please. *Pretty please.*

TAXABLE	Initial Cash	Profit on Flip	Tax on Profit	Cash Balance	NON-TAXABLE	Initial Cash	Profit on Flip	Cash Balance
1	$ 100,000	$ 30,000	$ 10,500	$ 119,500	1	$ 100,000	$ 30,000	$ 130,000
2	$ 119,500	$ 35,850	$ 12,548	$ 142,803	2	$ 130,000	$ 39,000	$ 169,000
3	$ 142,803	$ 42,841	$ 14,994	$ 170,649	3	$ 169,000	$ 50,700	$ 219,700
4	$ 170,649	$ 51,195	$ 17,918	$ 203,926	4	$ 219,700	$ 65,910	$ 285,610
5	$ 203,926	$ 61,178	$ 21,412	$ 243,691	5	$ 285,610	$ 85,683	$ 371,293
6	$ 243,691	$ 73,107	$ 25,588	$ 291,211	6	$ 371,293	$ 111,388	$ 482,681
7	$ 291,211	$ 87,363	$ 30,577	$ 347,997	7	$ 482,681	$ 144,804	$ 627,485
8	$ 347,997	$ 104,399	$ 36,540	$ 415,856	8	$ 627,485	$ 188,246	$ 815,731
9	$ 415,856	$ 124,757	$ 43,665	$ 496,948	9	$ 815,731	$ 244,719	$ 1,060,450
10	$ 496,948	$ 149,084	$ 52,180	$ 593,853	10	$ 1,060,450	$ 318,135	$ 1,378,585

Such is the power of compounding. Such is the cost of lost compounding when government takes money from the productive to ensure its own power.

"But this example is unrealistic"

- "That rate of return is too high"
  - I have clients who have consistently achieved far better rates of return. I have watched investors double their money on some rehabs. Based on having seen thousands of deals via tax returns and books I have reviewed for clients over two decades, a 30% return on a six-figure rehab & retail deal is quite realistic. If you cannot achieve such numbers….I'd get some education on the subject and improve on your present skill set.

- "An IRA would have to pay special IRA taxes known as UBIT on the rehab & retail deals"
  - Maybe, maybe not. We'll deal with that topic later on. Let's keep things simple for the moment. The primary point is that tax-free growth is very, very powerful and involves keeping very large sums of money in your hands – and out of the hands of politicians and bureaucrats.

- "My IRA doesn't have $100,000"
  - I didn't have the cash to buy my residence. I borrowed. Your IRA can borrow or partner to raise the necessary funds. See Example #4 for a very powerful & real-world example of how a small IRA can grow into a very large IRA. Again, remember the real point of

this example: Tax-free compounding increases your wealth by far, far more than is intuitive. Taxes *kill* compounding.

Here's a second, more modest example: Instead of rehabbing & retailing houses, we lend the IRA's money at hard money rates, say at 12%.[7] A 35% federal + state income tax rate applies. After ten years, taxable interest income would result in a $211,928 cash balance. Tax-free growth would result in a $310,585 cash balance, for a difference of $98,657. After 20 years the difference is even more extreme. The taxed growth would result in a cash balance of $449,133. Untaxed growth would result in a cash balance of $964,629. The $515,496 would go to the government. Don't worry, I'm sure those honest politicians and efficient bureaucrats "invested" your **seized money and lost growth** in something very useful. For the more numerically inclined, here's my math:

TAXABLE	Initial Cash	Profit on Flip	Tax on Profit	Cash Balance	NON-TAXABLE	Initial Cash	Profit on Flip	Cash Balance
1	$ 100,000	$ 12,000	$ 4,200	$ 107,800	1	$ 100,000	$ 12,000	$ 112,000
2	$ 107,800	$ 12,936	$ 4,528	$ 116,208	2	$ 112,000	$ 13,440	$ 125,440
3	$ 116,208	$ 13,945	$ 4,881	$ 125,273	3	$ 125,440	$ 15,053	$ 140,493
4	$ 125,273	$ 15,033	$ 5,261	$ 135,044	4	$ 140,493	$ 16,859	$ 157,352
5	$ 135,044	$ 16,205	$ 5,672	$ 145,577	5	$ 157,352	$ 18,882	$ 176,234
6	$ 145,577	$ 17,469	$ 6,114	$ 156,932	6	$ 176,234	$ 21,148	$ 197,382
7	$ 156,932	$ 18,832	$ 6,591	$ 169,173	7	$ 197,382	$ 23,686	$ 221,068
8	$ 169,173	$ 20,301	$ 7,105	$ 182,369	8	$ 221,068	$ 26,528	$ 247,596
9	$ 182,369	$ 21,884	$ 7,659	$ 196,593	9	$ 247,596	$ 29,712	$ 277,308
10	$ 196,593	$ 23,591	$ 8,257	$ 211,928	10	$ 277,308	$ 33,277	$ 310,585
11	$ 211,928	$ 25,431	$ 8,901	$ 228,458	11	$ 310,585	$ 37,270	$ 347,855
12	$ 228,458	$ 27,415	$ 9,595	$ 246,278	12	$ 347,855	$ 41,743	$ 389,598
13	$ 246,278	$ 29,553	$ 10,344	$ 265,487	13	$ 389,598	$ 46,752	$ 436,349
14	$ 265,487	$ 31,858	$ 11,150	$ 286,195	14	$ 436,349	$ 52,362	$ 488,711
15	$ 286,195	$ 34,343	$ 12,020	$ 308,519	15	$ 488,711	$ 58,645	$ 547,357
16	$ 308,519	$ 37,022	$ 12,958	$ 332,583	16	$ 547,357	$ 65,683	$ 613,039
17	$ 332,583	$ 39,910	$ 13,968	$ 358,525	17	$ 613,039	$ 73,565	$ 686,604
18	$ 358,525	$ 43,023	$ 15,058	$ 386,489	18	$ 686,604	$ 82,392	$ 768,997
19	$ 386,489	$ 46,379	$ 16,233	$ 416,636	19	$ 768,997	$ 92,280	$ 861,276
20	$ 416,636	$ 49,996	$ 17,499	$ 449,133	20	$ 861,276	$ 103,353	$ 964,629

Here's a third and pretty typical example: Investor does one rehab & retail deals in his IRA for 7 years with a fairly modest 30% return, and then slows down and lends the cash out at 12% for 13 years. After 10 years, the taxed cash balance is $435,945. The untaxed cash balance is $881,571, for a difference of $445,627. After 20 years, the taxed balance equals $923,888, while the untaxed balance equals $2,738,027 for a difference of $1,814,139. Here's the math:

[7] I have seen much "harder" rates, 5 points and 15%, for example. 12% is a very realistic number.

TAXABLE	Initial Cash	Profit	Tax on Profit	Cash Balance	NON-TAXABLE	Initial Cash	Profit	Cash Balance
1	$ 100,000	$ 30,000	$ 10,500	$ 119,500	1	$ 100,000	$ 30,000	$ 130,000
2	$ 119,500	$ 35,850	$ 12,548	$ 142,803	2	$ 130,000	$ 39,000	$ 169,000
3	$ 142,803	$ 42,841	$ 14,994	$ 170,649	3	$ 169,000	$ 50,700	$ 219,700
4	$ 170,649	$ 51,195	$ 17,918	$ 203,926	4	$ 219,700	$ 65,910	$ 285,610
5	$ 203,926	$ 61,178	$ 21,412	$ 243,691	5	$ 285,610	$ 85,683	$ 371,293
6	$ 243,691	$ 73,107	$ 25,588	$ 291,211	6	$ 371,293	$ 111,388	$ 482,681
7	$ 291,211	$ 87,363	$ 30,577	$ 347,997	7	$ 482,681	$ 144,804	$ 627,485
8	$ 347,997	$ 41,760	$ 14,616	$ 375,141	8	$ 627,485	$ 75,298	$ 702,783
9	$ 375,141	$ 45,017	$ 15,756	$ 404,402	9	$ 702,783	$ 84,334	$ 787,117
10	$ 404,402	$ 48,528	$ 16,985	$ 435,945	10	$ 787,117	$ 94,454	$ 881,571
11	$ 435,945	$ 52,313	$ 18,310	$ 469,949	11	$ 881,571	$ 105,789	$ 987,360
12	$ 469,949	$ 56,394	$ 19,738	$ 506,605	12	$ 987,360	$ 118,483	$ 1,105,843
13	$ 506,605	$ 60,793	$ 21,277	$ 546,120	13	$ 1,105,843	$ 132,701	$ 1,238,544
14	$ 546,120	$ 65,534	$ 22,937	$ 588,717	14	$ 1,238,544	$ 148,625	$ 1,387,170
15	$ 588,717	$ 70,646	$ 24,726	$ 634,637	15	$ 1,387,170	$ 166,460	$ 1,553,630
16	$ 634,637	$ 76,156	$ 26,655	$ 684,139	16	$ 1,553,630	$ 186,436	$ 1,740,066
17	$ 684,139	$ 82,097	$ 28,734	$ 737,502	17	$ 1,740,066	$ 208,808	$ 1,948,874
18	$ 737,502	$ 88,500	$ 30,975	$ 795,027	18	$ 1,948,874	$ 233,865	$ 2,182,739
19	$ 795,027	$ 95,403	$ 33,391	$ 857,039	19	$ 2,182,739	$ 261,929	$ 2,444,667
20	$ 857,039	$ 102,845	$ 35,996	$ 923,888	20	$ 2,444,667	$ 293,360	$ 2,738,027

If you want to have some fun, run the numbers over 40 years. The difference is simply hard to believe, but oh-so-true. Indeed, by the end of this publication I hope to have persuaded you that the proper frame of reference is closer to a century[8] – run *those* numbers, preferably while sitting down.

The tax savings have only begun, I am not yet done. Let's continue with the third example, above, where the investor rehabbed and retailed for a year in his Roth for seven years and then made hard-money loans for the next thirteen years, accumulating a balance of $2,738,027 in his Roth IRA. Let's assume that the IRA owner was 40 when he started investing via the Roth. As such, he'd be 60 with a Roth balance of $2.7M.

Instead of growing the account, let's assume that our investor/IRA beneficiary decided to start taking the interest income out of the IRA (aka "distributing" it) in order to live off of it. Perhaps he's getting a bit more laid back, wants the income to be more passive, and so he drops his rates to 10%. In that case, he'd be pulling $273,803 per year from the Roth. Because he has used a Roth IRA instead of a Traditional IRA, the distributions would be **100% tax-free to him**. At a 35% tax rate, his tax would have been $95,831 per year. Let's assume he lives to the happy age of 90. 30 years of saving $95,831 per year would equate to an additional $2,874,929 in tax savings. Adding that to the $1,814,139 extra cash we have due to tax-free growth, using the Roth has saved him $4,689,068. And remember, we could add quite a lot to that number if we choose to have the Roth outlive its owner.[9]

Example #4: "But my IRA only has <fill in your number>"

I know someone who used the technique below to acquire over fifty free and clear rentals in his Roth IRA. He is over 59.5 years of age. All of that rental income is therefore tax-free to him.

[8] To repeat my prior hint: Your Roth IRA can live on after you pass on. For example, your great-grandchild can inherit it and use it tax free for 60+ years.
[9] More on that later.

Step one: You are 40 years old. You contribute $5,500 to your Roth IRA. You never contribute another nickel.

Big deal, right? How is contributing $5,500 per year to going to save me millions in taxes? The math seems....off. Oh, the math works. Trust the nice lawyer and read on.

Step two: The Roth IRA purchases a rental for $27,000, all in, including rehab, closing costs, etc. The rental produces $675/month in rental income. Expenses average 40% of the rent, or $270. Net rental income/net cash flow per month averages $405 ($675 - $270) or $4,860 per year.

How did an IRA with $5,500 purchase a rental property for $27,000? It borrowed 100% of the money.[10] The terms of the loan were as follows:

- $27,000 borrowed. We are keeping our $5,000 contribution high & dry as a reserve.
- 6.75% interest
- 8 years, fully amortizing

In its first year, the rental brings in net cash of $4,860 (Gross rents of $8,100 less expenses of $3,240). It makes loan payments of $4,377 ($364.76 x 12). It also pays a special tax called UBIT of $306 (more on that later, trust me for just a little bit). $4,860 less $4,377 less $306 = $177 of cash at year end, without having touched our $5,000 reserve. Here's how it breaks down for all 8 years:

Year	Age	Net Rental Income	Loan Payments	UBIT	End of Year Cash	Loan Balance
1	40	$ 4,860	$ (4,377)	$ (306)	$ 177	$ 24,364.84
2	41	$ 4,860	$ (4,377)	$ (333)	$ 327	$ 21,546.20
3	42	$ 4,860	$ (4,377)	$ (363)	$ 447	$ 18,531.31
4	43	$ 4,860	$ (4,377)	$ (407)	$ 523	$ 15,306.49
5	44	$ 4,860	$ (4,377)	$ (463)	$ 543	$ 11,857.14
6	45	$ 4,860	$ (4,377)	$ (523)	$ 503	$ 8,167.62
7	46	$ 4,860	$ (4,377)	$ (587)	$ 398	$ 4,221.20
8	47	$ 4,860	$ (4,377)	$ (656)	$ 225	$ 0.00

At the end of eight years, you are 48 years old and the Roth IRA now has one free and clear property plus $5,225 in cash. There are no loan payments and no more UBIT tax. The property cash flows $4,860 per year.

Let's assume that the IRA cash flows that way for the next 12 years until you are 60. $4,860 x12 = $58,320. $58,320 + the $5,225 cash balance = $63,545.

Here's the nice thing about a Roth. At age 59.5, you can pull money out of it tax-free. Not tax-deferred. Tax-free. You pull out $58,545, leaving the rental property and a $5,000 cash reserve in the Roth. Let's assume you'll kick off at 90. You pull $4,860 of net rental income out of the Roth per year. 30 x $4,860 = $145,800. So over your life, you pulled $204,345 ($145,800 + $58,545) out of the IRA completely tax free – on one small rental house that was acquired for $27,000 all in.

Now do it 50+ times. Heck just do it 10 times – good enough!

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[10] Other rules that you have not yet learned about were involved. For example, the debt would need to be non-recourse and none of the private lenders could be "disqualified parties". More on that later.

"This example is unrealistic"

You're right, it is. I was conservative when I laid it out, one could really do much better. Specifically:

- I have seen investors who consistently buy low income rentals for significantly less.
  - Where should your best, cherry-picked deals go? In your taxable regular business, or in a non-taxable Roth IRA?
- I have seen investors with expenses consistently lower than was the case in my example
- None of the income or profits were reinvested or compounded (this is huge)
- Rents never went up
- The house did not appreciate
- There are ways to avoid the UBIT tax altogether (more on that later)
- We only contributed $5,000, one time, and never invested it or used it to generate income, it functioned solely as a reserve
  - Some types of retirement accounts allow you to contribute up to $53,000 per year. Every year.
- This example did not include a spouse's retirement account
- This example did not include the benefit of your great-granddaughter (for example) inheriting at age ten and pulling tax-free income from it until she hit sixty or so years of age.

Do I have your attention?

People often lie. Numbers do not. **If these numbers fail to convince you to take immediate action and to change how you do things (e.g. - to do at least some of your investing via a self-directed IRA and/or a self-directed 401k, especially via a Roth version of either account), then nothing I can do or say shall *ever* sway you.** Just shred this course, give Caesar more than he is due, and move on. For the rest of you....this information is only of value if you **act** in a thoughtful and disciplined manner.