

# DSTS – AN INTRIGUING ARMCHAIR INVESTMENT FOR 1031

*Delaware Statutory Trusts: An Option to Keep on Your 1031 Radar*

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In today's 1031 Exchange market, Delaware Statutory Trusts (DSTs) may offer an intriguing option for investors who are looking for properties to complete their 1031 Exchanges.

Why? DSTs are passive management/current income investment opportunities where investors do not have the typical responsibilities associated with actively managing investment properties. Also DST investment offers a convenient and timely 1031 Replacement Property solution when the market for traditional commercial/investment properties is tight.

## **What is a DST 1031 Exchange?**

A DST 1031 Exchange is where the investor sells their current investment property and completes their 1031 Exchange by purchasing DST interests as their Replacement Property. Read the how to specifics in [How to Identify DST Properties in 1031 Exchanges](#).

## **What is a DST?**

A DST is a legal entity created as a trust under Delaware law that holds one or more pieces of real property in which investors can purchase an ownership interest. The property(ies) are held, managed, administered, and/or operated for profit by a trustee for the benefit of the holders of the DST, creating a passive investment opportunity for the investor. A DST may consist of a varied or targeted portfolio of property types, sponsors, geographical locations and asset classes such as student housing, storage facilities, apartment buildings, hotels, drugstores, office buildings, or health care facilities.

According to DST proponents, these are some of the benefits of DST ownership:

- DSTs may offer higher quality, investment-grade assets that are typically only available to large institutions
- DSTs provide investors with income via cash distribution potential
- DST packages offer convenience for exchangers for specific amounts of investment, speed and certainty of close for Replacement Property
- DST fractional ownership allows investors to diversify their capital to invest across multiple DST offerings
- DST investors do not need to manage or participate in day-to-day operations
- DST debt is non-recourse, which means that in the event of a default, DST investors are not personally liable

## **How Does a DST Work?**

A trustee of the DST initially purchases the property and takes title. The sponsor of the DST, the party who typically arranges the bank financing and coordinates the management of the property, then structures the transaction and arranges for sale of beneficial interests to individual investors. Though the beneficial interests are considered to be securities under federal securities laws, for purposes of 1031 Exchanges, Revenue Ruling 2004-86 states that a beneficial interest in a DST is considered "like-kind" real estate.

Of course, DSTs are not suited for all. Investors who enjoy managing the day-to-day operations of their properties may not be good candidates. A DST is also not for an investor who wishes to invest in property for a short period since DST investments are typically designed for a holding period of 2 to 10 years or more. Additionally, DSTs are designed for "accredited investors" which are high net worth individuals as defined by the SEC. And with all investments, the fees need to be considered.

Given the intricacies of purchasing suitable real estate assets and structuring these offerings from both a securities and tax perspective, exchangers and their financial advisors should perform due diligence to determine if a DST is right for their investment situation. The DST sponsor will provide a Private Placement Memorandum ("PPM") which provides information about the properties, area demographics, leases, projections and other important disclosures. Due diligence emphasis should be placed on real estate, property management and asset management expertise, prior performance track record, experience with sophisticated financing structures, transparent investor communications, financial strength of the sponsor and excellent legal representation.

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