



Podium

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Ownership options key in investment properties

If you decide to pool your resources with other investors to buy a rental property, you may be considering various ownership options, including joint ventures, limited partnerships, bare trusts or corporations. Each option will have different implications for you throughout the life of your real estate investment. These include tax treatment, ease of entry or exit (liquidity), control and protection from personal liability.

The first step is to ensure that when you make an offer on a property, it contains a right of assignment so you have the most flexibility in choosing an ownership structure.

Any ownership structure will be based on an agreement that sets out the rights and obligations between investors, such as those outlined in a limited partnership or joint venture agreement. These agreements address who controls the property, how decisions are made, how funds are raised, who is liable for guarantees or financial contributions, how people can exit the investment and how profits are distributed.

Personal liability, or avoiding it, is an important consideration. Many lenders require a personal guarantee on the mortgage, leaving investors exposed to unlimited liability for the debt. Investors can still own the property through a company or other entity to limit financial liability to third parties for debts, or risks, such as personal injury or environmental hazards on

the property. Unless you are doing substantial development, these liabilities to third parties, beyond typical insurance coverage, may be relatively minor in comparison to the mortgage.

Tax planning often determines which ownership structure you choose. Income and losses in a firm stay within the firm (profit may be split among shareholders), while an individual in a partnership or joint venture will take the income or losses personally. Also, property transfer tax can be reduced where a beneficial (partnership or joint venture) interest is sold rather than selling the property itself.

Many rental properties incur losses the first few years. Investors often want a personal interest in the property, so they can use the losses to reduce other taxes. Limited partnerships are popular for this reason, because they give personal ownership with limited liability protection.

A limited partnership is made up of a general partner — which bears the risk for the liabilities — and limited partners, whose risk is limited to the maximum investment obligation they have agreed to make. All business must be controlled and conducted through the general partner — often a company — otherwise the limited liability protection may be lost.

If all of the investors intend to manage the property, a limited partnership may not be appropriate. Although limited partners may also be companies, the tax benefit of the losses will go into the company, not the individuals. Selling a limited partnership interest will not likely trigger property transfer tax, but finding a new investor for the existing ownership structure may not be as simple as selling the property itself.

A joint venture is a common real estate investment structure. This is not a partnership, but is a special relationship for the co-ownership of a particular property. Unlike a partnership, participants in a joint venture cannot

bind their counterparts in business arrangements outside of the joint venture. Investors can be corporate or individual. Any of the participants can manage and control the investment and all risk is shared by the joint venture participants. All tax consequences flow through to the joint venture participants because the joint venture is not a taxable entity.

A joint venture can be organized more simply, in many cases, than a limited partnership, and exiting the joint venture can be as simple or as complex as the parties determine in their agreement.

Pooled investments may be regulated by securities laws and you should obtain legal advice before participating in or organizing one.

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