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Planning for a co-owner's woes

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NORTH BAY -- One unresolved legal question regarding the increasingly touted tenant-in-common real estate investment strategy is the question of what happens if one of the tenant-in-common investors goes bankrupt.

The IRS only began to generally allow so called TICs as 1031 replacement properties with a revision to the tax code in 2002.

Given the relative youth of these investments, some of the legal niceties have yet to be ironed out, explains Napa tax attorney Stan Blyth, a partner at Dickenson, Peatman & Fogarty.

One of these is what the impact would be on other TIC investors in a property should one TIC investor file for bankruptcy.

"That's a big open question right now," Mr. Blyth says.

The IRS allows up to 35 different individuals to co-own a real estate investment as tenants in common, he notes.

But unlike the owner of a condominium, who owns a specific, divided portion of a larger property, the tenant in common owns an "undivided interest" in the entire property, explains Blyth's partner Matthew Eisenberg.

While this distinction ensures the benefits of owning the property will be shared equally among the tenants in common, Mr. Eisenberg says it also could make it harder for each of them to distance themselves from one of their co-owner's legal woes.

The bankruptcy of a fellow tenant in common might mean liens could be placed on each of the other investors' interests in the property as well, Mr. Blyth explains. This could have numerous ramifications for investors' ability to sell their individual interests, the owners' plans to refinance the property, and the manager's efforts to lease space in the property, he adds.

At least one broker involved in such transactions says these questions are valid and help bring a note of sobriety to the enthusiasm with which such exchanges are often marketed.

"There is kind of this attitude out there that these are super great investments with no risk, and obviously that's not always true," says Adam Skarsgard, national sales manager at Walnut Creek-based North American Exchange Company.



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