Educational Handbook

Delaware Statutory Trusts (DSTs)

About CAI Investments LLC

CAI Investments, LLC is a vertically integrated real estate development company headquartered in Las Vegas, NV. Since its formation in 2011 by Christopher Beavor, CAI has financed, developed, and managed commercial properties in key markets across the United States. Its primary focus is to find quality assets in desirable locations while working with publicly-traded national brands such as Marriott, Del Taco, Walgreens, Starbucks, etc. to add value to its clients. CAI's current portfolio includes industrial, hospitality, office, quick service restaurants, and mixed-use assets.

+/- $1.8 Billion in AUM

Our mission statement is:

'Developing Trust through Transparency and Vision'

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Introduction to Delaware Statutory Trusts (DSTs)

What is a DST?

A **Delaware Statutory Trust (DST)** is a distinct legal entity created under Delaware state law. It is commonly used in real estate investment, particularly for large commercial properties, where multiple investors can own fractional interests in a property without direct management responsibilities.

The DST structure enables investors to pool their funds into a trust that owns one or more properties, such as apartment complexes, office buildings, retail centers, or industrial properties. Each investor holds a "beneficial interest" in the trust, entitling them to a proportional share of the income generated by the property and any potential appreciation.

History and Legal Framework

DSTs were formally recognized in 1988 under Delaware state law. However, it wasn't until 2004 that the IRS issued Revenue Ruling 2004-86, clarifying that DSTs can qualify as "like-kind" properties for 1031 exchanges. This ruling positioned DSTs as a preferred investment vehicle for investors looking to defer capital gains taxes through 1031 exchanges.

How DSTs Work

Structure of a DST

A DST is typically established by a sponsor, which is a company that identifies and acquires real estate assets for the trust. The sponsor structures the DST, manages the property, and offers fractional ownership interests to individual investors.

- **Sponsor:** Responsible for identifying, acquiring, and managing the property held by the DST.
- **Trustee:** Oversees the trust's operations, ensuring compliance with legal requirements.
- **Investors:** Individuals who purchase beneficial interests in the DST. They receive income distributions based on the rental income generated by the property, as well as potential profits from the eventual sale.

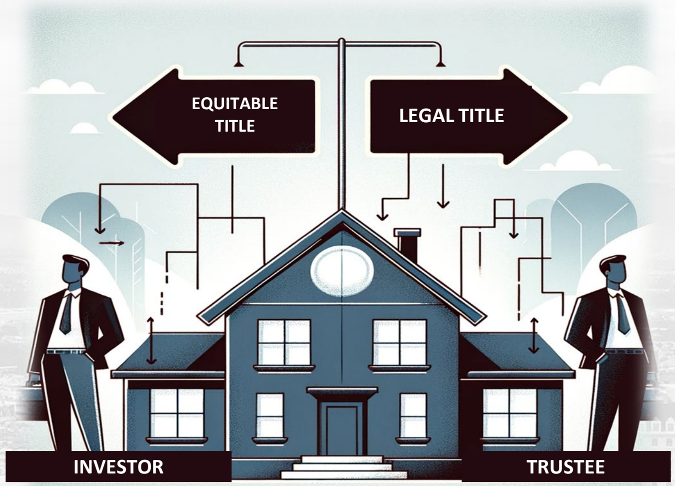
Roles in a DST: Sponsors, Trustees, and Investors

- **Sponsors:** The sponsor's role includes acquiring the real estate, structuring the DST, and managing all aspects of the property, from leasing to eventual sale. Sponsors typically offer DST investments to accredited investors.
- **Trustees:** The trustee is a fiduciary responsible for the legal and financial administration of the trust. The trustee ensures that the DST remains in compliance with the terms of the trust agreement and Delaware statutory law.
- **Investors:** Investors in a DST are passive owners. They are not involved in day-to-day management or decision-making regarding the property but receive income distributions proportionate to their investment.

Beneficial Interest in a DST

When investors purchase an interest in a DST, they are acquiring a "beneficial interest" rather than direct ownership of the property. This beneficial interest gives investors the right to:

- Receive a share of the income produced by the property.
- Benefit from depreciation and other tax advantages.
- Share in the proceeds from the eventual sale of the property.



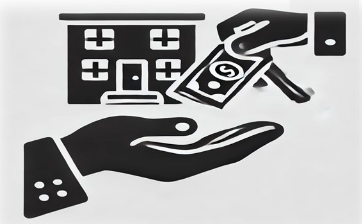
Key Benefits of DSTs

- **Passive Investment Opportunity:** One of the most significant advantages of DSTs is the **passive nature** of the investment. Investors do not need to be involved in the day-to-day management of the property. The sponsor handles all operational aspects, including leasing, maintenance, and property improvements.
- **Proportionate Distributions:** Unlike most LLC investments, a DST program requires proportionate distributions, so the sponsor will not receive a "promote" on investor's returns
- **Access to Institutional-Grade Assets:** Through a DST, individual investors gain access to large, high-quality commercial properties that they may not have been able to purchase on their own. These can include large apartment complexes, office buildings, retail centers, and industrial assets.
- **Diversification:** Investors can diversify their portfolios by investing in multiple DSTs that offer exposure to different property types and geographic locations. This diversification can help mitigate risks and improve returns.
- **Predictable Income**: DSTs are structured to provide **consistent cash flow** through regular income distributions. These distributions come from the rental income generated by the property, which is particularly attractive to investors seeking passive income.
- **Tax Advantages**: In addition to regular income, DSTs offer significant tax advantages, including:
  - **Depreciation**: Investors can claim depreciation on their share of the property, reducing taxable income.
  - **1031 Exchange Eligibility**: DSTs qualify as like-kind properties for 1031 exchanges, allowing investors to defer capital gains taxes when selling one property and purchasing another through a DST.

Eligibility of DSTs for 1031 Exchanges

- **DSTs as Like-Kind Properties:** A key reason why DSTs are popular among real estate investors is that they qualify as **like-kind properties** under the IRS's 1031 exchange rules. This means that an investor can sell real estate held for investment, defer capital gains taxes, and reinvest the proceeds into a DST through a 1031 exchange.
- **Deferred Taxes Through a 1031 Exchange:** By exchanging into a DST, investors can continue deferring taxes on capital gains, depreciation recapture, and other taxable events, allowing their wealth to grow untaxed until they choose to cash out or pass the assets to heirs.

DST Investment Lifecycle



- **Acquisition Phase:** The sponsor identifies a property, acquires it, and establishes the DST. Once the DST is formed, the sponsor raises capital by offering fractional ownership to investors.

- **Holding Period:** DST investments typically have a holding period ranging from 5 to 10 years, during which the property is leased to tenants, and investors receive regular income distributions. The sponsor handles property management, while investors receive passive income.

- **Exit Strategy and Distribution of Sale Proceeds:** At the end of the holding period, the sponsor will sell the property. Investors then receive their share of the sale proceeds, which may include both their initial investment and any profits. Investors may choose to perform another 1031 exchange into a new DST or cash out and pay taxes on the deferred gains.

Risks and Limitations of DSTs

While DSTs offer many benefits, they also come with some risks and considerations

- **Illiquidity:** Once you invest in a DST, your funds are typically locked in until the property is sold, which can take several years.
- **Lack of Control:** Investors in DSTs do not have any management authority. The sponsor manages all aspects of the property, from leasing to eventual sale.
- **Property Performance:** Like any real estate investment, the performance of a DST property is subject to market conditions and other factors that may affect its income and value.
- **Restrictions on Refinance:** Generally DSTs sell the property instead of refinancing because a refinance could adversely impact the 1031 of investors.

Comparing DSTs with Other Investment Structures

- **DSTs vs. Tenant-in-Common (TIC)**
  - **Management:** DSTs offer fully passive management, whereas TIC investors often have active roles in decision-making.
  - **Number of Investors:** DSTs allow an unlimited number of investors, while TICs are limited to 35 co-owners.
  - **Financing:** Generally DSTs sell the property instead of refinancing because a refinance could adversely impact the 1031 of investors, while TICs can refinance, although this can be more complicated due to shared ownership.
- **DSTs vs. Real Estate Investment Trusts (REITs)**
  - **Ownership:** DST investors hold ownership interest in REAL property while REIT investors do not.
  - **Liquidity:** REITs are more liquid than DSTs, as they can be traded on stock exchanges.
  - **Tax Benefits:** DSTs allow for 1031 exchange tax deferral, while REITs do not.

Who Should Consider Investing in DSTs?

- **Ideal Profiles of DST Investors**
  - **1031 Exchange Investors:** DSTs are an attractive option for investors looking to defer capital gains taxes through a 1031 exchange.
  - **Passive Income Seekers:** Investors looking for consistent income without the hassle of property management may benefit from DSTs.
  - **Accredited Investors:** DST investments are often offered to accredited investors, meaning those who meet specific income or net worth criteria.
- **When DSTs Might Not Be Suitable**
  - **Investors Seeking Liquidity:** If you need quick access to your investment funds, DSTs may not be the best option due to their illiquid nature.
  - **Active Managers:** Investors who prefer hands-on involvement in managing real estate may find DSTs too passive and limiting.

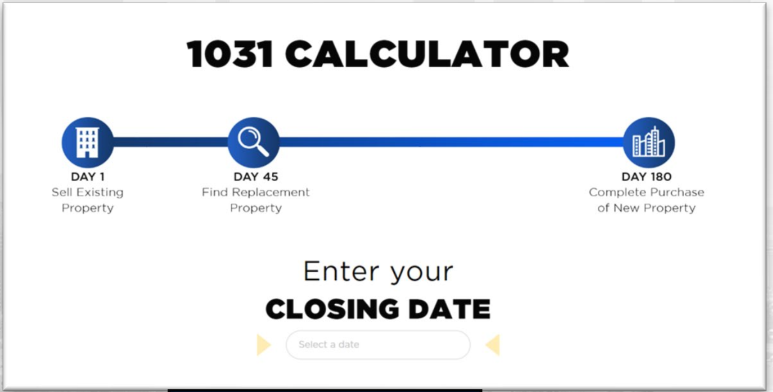
Frequently Asked Questions (FAQs)

- **Can I exchange multiple properties into a DST?**
  - Yes, you can consolidate multiple relinquished properties into a single DST, provided the transaction meets IRS 1031 exchange requirements.
- **What happens at the end of the DST's holding period?**
  - The sponsor will sell the property, and investors will receive their share of the proceeds. At that point, you can either reinvest in another DST or a new property through a 1031 exchange.
- **What types of properties do DSTs typically hold?**
  - DSTs can hold a variety of commercial real estate assets, including multifamily properties, office buildings, industrial facilities, and retail centers.

Conclusion

A **Delaware Statutory Trust (DST)** offers a unique opportunity for real estate investors seeking a passive, tax-advantaged investment in institutional-grade properties. Through the fractional ownership model, investors can diversify their portfolios, earn consistent income, and defer taxes through 1031 exchanges. However, investors should be mindful of the illiquidity, lack of management control, and market risks associated with DST investments.

By understanding the benefits, risks, and structure of DSTs, you can make informed decisions to align your real estate investment strategy with your financial goals. Always consult with financial and tax professionals to ensure that DST investments fit within your overall portfolio and long-term strategy.



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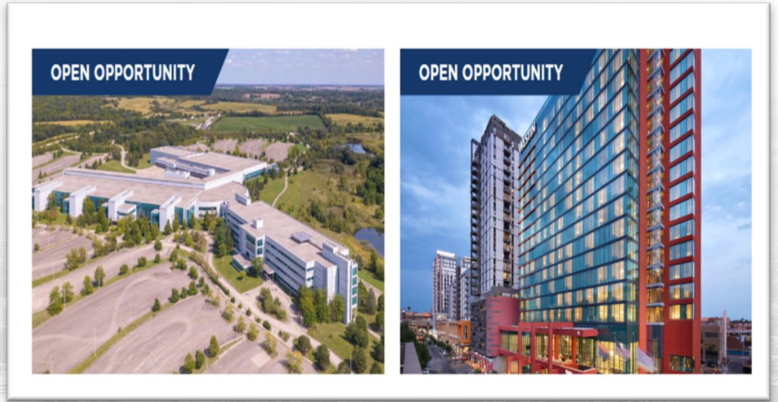

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Disclaimers

Important Disclosure: Information and numerical examples are for educational purposes only and do not constitute an offer to purchase or sell securitized real estate investments. DST 1031 properties are only available to accredited investors (typically have a $1 million net worth excluding primary residence or $200,000 income individually/$300,000 jointly of the last three years) and accredited entities only. If you are unsure if you are an accredited investor and/or an accredited entity please verify with your CPA and Attorney. There are risks associated with investing in real estate and Delaware Statutory Trust (DST) properties including, but not limited to, loss of entire investment principal, declining market values, tenant vacancies, and illiquidity. Potential cash flows/returns/appreciation are not guaranteed and could be lower than anticipated. Because investors' situations and objectives vary this information is not intended to indicate suitability for any particular investor. This material is not to be interpreted as tax or legal advice. Please speak with your own tax and legal advisors for advice/guidance regarding your particular situation

<u>1031 Risk Disclosure:</u>

- There is no guarantee that any strategy will be successful or achieve investment objectives including, among other things, profits, distributions, tax benefits, exit strategy, etc.;
- Potential for property value loss – All real estate investments have the potential to lose value during the life of the investments;
- Change of tax status – The income stream and depreciation schedule for any investment property may affect the property owner's income bracket and/or tax status. An unfavorable tax ruling may cancel deferral of capital gains and result in immediate tax liabilities;
- Potential for foreclosure – All financed real estate investments have potential for foreclosure;
- Illiquidity – These assets are commonly offered through private placement offerings and are illiquid securities. There is no secondary market for these investments.
- Reduction or Elimination of Monthly Cash Flow Distributions
  – Like any investment in real estate, if a property unexpectedly loses tenants or sustains substantial damage, there is potential for suspension of cash flow distributions;
- Impact of fees/expenses – Costs associated with the transaction may impact investors' returns and may outweigh the tax benefits
- Stated tax benefits – Any stated tax benefits are not guaranteed and are subject to changes in the tax code. Speak to your tax professional prior to investing.

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