



INVESTING GUIDE

PRIVATE DEBT INVESTING WITH A SELF-DIRECTED IRA

Diversifying your retirement portfolio, made easy.



Self-directed IRAs offer access to a wide range of investment options including private debt.

Private debt is a unique opportunity for investors to capitalize on debt that's incurred by individuals, companies and corporations of varying sizes. What makes this opportunity so distinctive when held in an IRA (or self-directed IRA) is that you have the ability to purchase the debt and collect the interest — all on a tax-advantaged basis.

WHAT IS PRIVATE DEBT?

In the aftermath of the 2008 financial crisis, private debt has become an established asset class in its own right, matching the needs of yield-seeking investors and companies looking for capital to grow.

The financial crisis resulted in many traditional sources of funds for borrowers drying up. Even with the resurgence in the economy in recent years, private debt is still a source of funds for many borrowers seeking nontraditional financing solutions.

Within the private debt arena, there are many different types of opportunities available for investors. Let's look at some of the drivers for this growth and assess how investors can build on further opportunities in the private debt market by using a self-directed IRA.

WHY INVEST IN PRIVATE DEBT?

Private debt offers a number of advantages for investors in general and specifically when held inside of an IRA:

- Private debt can offer higher returns than traditional fixed income securities like bonds and CDs, offering enhanced return opportunities for investors.
- Private debt is largely uncorrelated with traditional asset classes like stocks or bonds. Your return is based upon the borrowers making interest and principal payments throughout the life of the loan.
- Private debt offers investors another way to access various alternative assets like real estate, infrastructure and corporate financing. With the stock market at or near all-time highs, private debt can offer a welcome level of diversification in your retirement portfolio.

TYPES OF PRIVATE DEBT INSTRUMENTS

There are many alternatives for investors looking for private debt opportunities. Here are a few that many of our clients at STRATA use.

Trust deeds and mortgage notes offer the opportunity to lend funds from your IRA through a promissory note secured by a deed of trust or mortgage to an unrelated third-party. The periodic interest and principal payments flow into your IRA account where they retain their tax-deferred (or tax-free in the case of a Roth account) status. In addition to the advantages of collecting the ongoing payments, you can resell the debt instrument to another purchaser offering a potential degree of liquidity to free up these funds for other investment opportunities within your IRA.

Secured notes represent debt that is secured by specific assets of the borrower. These assets could be equipment, real estate, interest in a business or other type of assets. The loan will be structured so that borrower makes scheduled interest and principal payments. The advantage is that if the borrower defaults, the loan is secured by specified, tangible assets that can either be sold and converted to cash or held by the lender. Used inside an IRA, all interest and principal payments remain tax-deferred (or tax-free with a Roth) until the funds are withdrawn in retirement.

Convertible notes are promissory notes or other forms of debt that convert into equity at some point in the future. These are typically short-term notes that will convert to equity at a specified milestone, often coinciding with the debtor company's next round of financing. The terms of the equity conversion often include a discount to the share price offered to investors in the next round of financing. There is generally a cap on the price at which your notes will convert to equity, providing the potential for upside if the stock does well when it opens for trading. An IRA provides an excellent vehicle for investing in convertible notes

in the event that the stock does well. Your capital gains will be shielded from taxes until retirement or remain tax-free if held in a Roth account.

Corporate debt offerings are instruments such as notes, bonds, or debentures used by corporations to borrow money. Through your IRA you can invest in corporate debt. The money is loaned from the IRA and interest is received into the account on a tax-advantaged basis.

These are some of the most common private debt arrangements, but there are certainly others. Generally, these private debt arrangements offer higher yields in exchange for the added risk investors in these notes assume, as well as for the lack of liquidity inherent in many of these deals.

TYPES OF PRIVATE DEBT NOT ELIGIBLE WITH STRATA

As a self-directed IRA custodian, we try to be as flexible as possible in helping accountholders to invest in private debt opportunities. We do have a few restrictions on private debt investments. These include unsecured loans to individuals, loans secured by an automobile title or loans secured by foreign real estate or personal property. We've found that these types of private debt arrangements can potentially be problematic for both accountholders and STRATA based upon our past experience.





A VISION FOR YOUR FUTURE

For more than a decade, STRATA Trust Company has helped thousands of investors and investment professionals hold a wide range of alternative investments in self-directed retirement accounts. We've built our reputation by delivering streamlined and straightforward custody, serviced by a team that is available to help and well-versed in regulatory requirements.

CHOOSE THE RIGHT CUSTODIAN

Working with a custodian that has a working knowledge of private debt transactions within a self-directed IRA account is critical.

WHY USE STRATA

STRATA offers investment flexibility beyond what most banks, brokerage firms and other financial institutions allow. We have a seasoned team with solid expertise in the custody of alternative assets including private debt. You can rest assured that STRATA has the know-how to handle your custody needs. In addition, STRATA offers customer focused technology that lets you complete, sign and electronically submit common IRA forms and most importantly we are available by phone or email to answer your questions. We'll take care of the details, giving you unmatched personalized service.

WHAT YOU SHOULD KNOW ABOUT PRIVATE DEBT

Here are a few things you should know about investing in private debt within your self-directed IRA account:

- Investors will need to hire a third-party debt servicing agent to monitor the terms and the collection of all payments associated with the debt. Alternatively, the investor can serve in that role if they wish.
- The debt agreement should clearly state the terms of the loan including the face amount, the term of the loan, the interest rate, the timing of interest payments and the maturity date.
- For secured private debt transactions, the accountholder should be sure the deed of trust or mortgage is properly recorded to secure the note.
- The debt arrangement should not constitute a prohibited transaction (see more on prohibited transactions in the section below).

WHAT IS A PROHIBITED TRANSACTION?

A prohibited transaction is the improper use of your IRA assets by you (the IRA owner), your beneficiary, or certain parties who are referred to as “disqualified persons.”

WHO IS A DISQUALIFIED PERSON?

- The IRA owner
- The spouse of the IRA Owner
- Any lineal descendants and their spouses
- Any lineal ascendants and their spouses
- Investment advisors and managers
- Anyone providing services to the IRA such as a trustee or custodian

NEXT STEPS

If you are ready to take the next step to add private debt to your retirement account, here's what you need to do:



STEP 1

Open your IRA online (or with our paper application)



STEP 2

Fund your account via rollover, a transfer or a contribution



STEP 3

Direct your investments

In addition, there are specific forms and documents that you will need to provide to STRATA before investing in a private debt arrangement. STRATA's Private Debt investment Checklist is easily accessible on our website www.StrataTrust.com, and our knowledgeable and experienced associates are here to help you every step of the way.

STRATA—THE CLEAR DIFFERENCE



STABILITY

Over 350 years of collective experience, 50+ employees, and more than a decade operating with direct oversight by the Texas Department of Banking.



SPEED

Streamlined processes and digital documentation and signing to facilitate speedy transactions and transfer of assets.



COMMUNICATION

Prompt and accurate communication on transaction status, statement updates and investment requests.



TECHNOLOGY

Secure and easy-to-use technology for straightforward account management, documents, tax statements and notifications.



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