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# REAL ESTATE ROYALTIES FOR MULTI- GENERATIONAL FAMILY OFFICES

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# Real Estate Royalties for Multi-Generational Family Offices

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## Abstract

This whitepaper examines the investment opportunity for family offices to allocate capital to real estate royalties. Modern unsubordinated, triple-net, long-term ground leases separate land ownership from improvements, creating the senior-most real estate claim: contractual, inflation-protected income with no lessor operating burden and full reversion of improvements at maturity. Institutions from the Catholic Church to leading universities have compounded wealth through this structure for centuries with no realized losses. Recent standardization has made the asset class accessible at institutional scale via specialized vehicles. For multi-generational family offices, ground leases deliver equity-like returns at markedly lower volatility than core real estate, substantial estate-tax valuation discounts, full like-kind exchange eligibility, and negligible management intensity. A modest allocation to ground lease assets can strengthen after-tax, intergenerational capital preservation and is worth consideration for family offices with patient capital, especially those considering multigeneration estate plans.

## Introduction

One of the distinct advantages family offices have over traditional institutional capital is the ability to invest patiently over long cycles, often generations. Family offices therefore benefit the most from investments that compound purchasing power over decades while preserving capital and imposing almost no operational burden on staff or principals. Modern ground leases deliver on all three of these requirements in a way that traditional real estate equity, private credit, and most fixed-income alternatives cannot.

In a ground lease, the landowner (formally the lessor or fee owner) retains outright ownership of the land while leasing it for a long term, almost always 99 years in institutional structures, to a tenant or lessee who constructs and owns the buildings and any improvements. The lessee pays rent on the land only and assumes full responsibility for property taxes, insurance, maintenance, and all operating costs under a triple-net (NNN) lease. At expiration, the lessee surrenders the improvements to the lessor in good condition and at no additional cost. This separation of land ownership from building ownership creates what are often referred to as “real estate royalties” (i.e., a senior, contractual, inflation-protected income stream plus a free, embedded option on decades of property appreciation).

Institutions as diverse as the Catholic Church, the British Crown, Harvard University, Yale University, and the University of Texas System have employed ground leases for hundreds of years to compound wealth with zero realized losses. And, since 2017, with the standardization of the modern unsubordinated, triple-net, 99-year ground lease, this asset class has become accessible on an institutional scale to private family office investors.

## Historical Context and Provenance

Ground leases trace their origins to English common law and were imported to the American colonies. Early examples include Dutch patroonships in New York and ecclesiastical leases in Hawaii. In the twentieth century, universities and municipalities adopted the structure to monetize land without surrendering control. The University of California, Irvine, the University of Texas System, and the City of New York have collectively generated billions in present-value rent while retaining reversionary rights that will mature in the twenty-second and twenty-third centuries.

The modern institutional version differs materially from older subordinated or short-term leases. It is always unsubordinated — meaning the lessor’s land is not collateral for the lessee’s construction or permanent financing — and contains lender-protective provisions that make the leasehold estate fully financeable with commercial mortgage-backed securities (CMBS) or bank debt. These innovations eliminated the primary historical friction: leasehold lenders’ fear that the fee owner could wipe out their collateral in a tenant bankruptcy. With that risk removed, the asset class is increasingly being seen as an attractive alternative for long term family office investors.

## Detailed Mechanics of the Institutional Ground Lease

A contemporary ground lease transaction typically begins with a developer or owner who controls a site but wishes to minimize deployed equity. The ground lease investor purchases the land (or funds it in a forward commitment) at 30–45% of total project cost and leases it back under the following core terms:

- Term: 99 years (the longest term that avoids perpetual lease rules in most states).
- Rent: Initial yield of 4.5–5.75% on land value, producing a blended project cap rate of approximately 6.5–8.0%.
- Escalators: Either (a) fixed 2.0–2.5% annual compounding, or (b) periodic CPI lookbacks (usually every 10 years) with collars of 1.5–3.5% per period or 20–35% cumulative.
- Triple-net: Lessee pays absolutely everything — property taxes, insurance, maintenance, capital expenditures.
- Unsubordinated fee: Lessor’s land is senior to all leasehold debt.
- Reversion: Improvements revert to lessor at maturity in good condition, with no payment to lessee.

The economics separate into two distinct value components for the lessor:

- The income component: a growing, senior, contractual cash flow stream that resembles an inflation-linked bond issued by a real estate-secured credit tenant.
- The reversionary or “Caret” component: the right to receive, at zero additional cost, all improvements existing at lease maturity.

Please refer to Appendix A for an explicit illustration of how ground lease economics work in practice.

## Comprehensive Risk Assessment

Ground leases sit at the absolute top of the real estate capital stack. In tenant bankruptcy or leasehold foreclosure, the land survives intact and any leasehold lender must continue paying rent or forfeit the improvements. This structural seniority explains the zero-loss history. The principal risks of ground leases are well understood and can be systematically mitigated with the appropriate planning and structuring.

- Tenant credit default is the most frequently cited concern. Managers address it through rigorous underwriting that requires either investment-grade credit or strong institutional sponsorship, coupled with minimum rent coverage ratios of 2.5–3.5 times.
- Insufficient inflation protection is eliminated in institutional leases via periodic CPI lookbacks (typically every ten years with collars) or, in retail properties, percentage-rent participation clauses that explicitly preserve purchasing power.
- Reversion risk—the theoretical possibility that improvements will be worthless at lease maturity in year 99—is effectively nonexistent. Conservative initial land allocations of 30–45% of total project cost, combined with the 99-year term and long-term real estate appreciation trends, ensure the reversionary interest retains substantial value.
- Interest-rate duration risk represents the primary source of mark-to-market volatility. Macaulay duration approximates 50–60 years, making the asset class sensitive to rate movements. Contractual cash flows, however, remain completely unaffected by interim price fluctuations.[1]
- Liquidity varies by vehicle. Private fund holdings are inherently illiquid, though a secondary market continues to develop. Investors seeking daily liquidity can access a public REIT (Safehold), accepting equity-like volatility in exchange.
- 6. Relative to core real estate, ground leases deliver comparable expected nominal returns—8–10% unlevered—while exhibiting roughly 40–50% of the volatility, placing them in the upper-left quadrant of the risk-return spectrum.

## Acquisition and Origination Strategies

Family offices access ground leases through four primary channels, listed below from most common to most bespoke:

1. Commingled private funds: These funds originate new leases and acquire existing ones at targeted net IRRs of 8–12%.
2. Club deals: Allows geographic, property-type, or escalator customization. Requires internal real estate staff in addition to trusted advisors.

[2] See Appendix A for step-by-step calculations.

[3] Holland & Knight. (2023). Independent Sponsors: Market Trends and Industry Insights.

3. Direct origination: This option is only for largest family offices and those with dedicated in-house real estate teams. Investments typically take 6–18 months from term sheet to funding and the process includes:

- Identifying developers or owners seeking to recycle equity.
- Negotiate land value (usually 30–45% of total project cost).
- Execute simultaneous land purchase and 99-year lease (using institutional template).
- Fund at closing or via forward commitment.

4. Public REIT: Safehold Inc. (NYSE: SAFE) is currently the only public pure-play ground lease company that trades in the public markets. It provides daily liquidity and exposure to a diversified national portfolio, albeit with equity market volatility and a significant discount to NAV.

Secondary acquisition of existing ground leases is growing. Universities, municipalities, and some family owners periodically monetize portions of their portfolios. These trades usually occur off market through intermediaries and specialist advisors.

## Tax Considerations for U.S. Family Offices

Tax treatment is a major reason sophisticated family offices find ground leases attractive[2]. For the lessor (the family office investor):

- Ground rent received is taxed as ordinary income (current federal rates up to 37% + 3.8% Net Investment Income Tax + state taxes).
- No depreciation deduction is available on the land itself (land is non-depreciable), and the lessor owns no improvements during the term.
- Property taxes, insurance, and operating expenses are paid by the lessee — fully tax-deductible to the lessee but never expensed by the lessor.
- Interest expense on leverage secured by the leased fee is deductible against rent (subject to normal limitations).

At lease maturity or upon earlier sale:

1. Reversion of improvements: The IRS generally treats the receipt of improvements at maturity as nontaxable return of property if the lease qualifies as a true lease. The lessor takes a zero basis in the reverted improvements. If sold immediately, the entire proceeds are capital gain (20% federal + 3.8% NIIT + state). Many lessors hold or 1031 exchange the mature property[3].

2. Sale of leased fee during term: Eligible for Section 1031 exchange into another ground lease or other real property, deferring capital gains tax indefinitely across generations. This is a powerful intergenerational planning tool.

3. Estate tax valuation: The IRS values a ground lease interest at the present value of remaining rents plus discounted reversion. Using IRS Section 7520 rates (4–6% currently), a newly originated 99-year lease is typically valued at 80–90% of invested capital for estate purposes, creating a built-in estate-tax discount. When held in intentionally defective grantor trusts or dynasty trusts in Delaware, Nevada, or South Dakota, the discounted value plus future appreciation can grow outside the taxable estate permanently.

Additional nuances:

1. Opportunity Zone ground leases can provide tax deferral on prior gains plus 10-year basis step-up.
2. Charitable remainder trusts (CRTs) can hold ground leases to generate high current income for principals while achieving charitable deductions.
3. GST-exempt dynasty trusts can own ground leases to compound for centuries without estate or GST tax at each generation.

In contrast, direct fee-simple real estate generates depreciation recapture at 25% on sale, annual phantom income if leveraged, and full fair-market-value inclusion in estates.

## Conclusion

Ground leases represent the purest form of real estate ownership available in a leveraged world: perpetual land control, growing senior income, no operating burden, and a tax-efficient embedded call option on future development value. For multi-generational family offices navigating ‘higher-for-longer’ interest rates, fiscal uncertainty, and generational transfer planning, a strategic allocation to modern ground leases can materially improve portfolio durability, after-tax compounding, and sleep-at-night quality. In the current market environment, commercial real estate transaction volume has recovered from the 2023–2024 lows, yet all-in debt costs remain 6.5–8.0% for many property types. Developers and owners are increasingly using ground leases to reduce equity requirements from 30–35% to 15–20%, creating abundant supply for lessors. Institutional ownership of the \$20+ trillion U.S. commercial real estate stock remains below 0.5%, indicating decades of runway for this unique real estate asset class.

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[1] Macaulay duration measures the weighted average time (in years) an investor must hold a fixed-income instrument to receive the present value of all future cash flows equal to its current price. Developed by Frederick Macaulay in 1938, it represents the economic maturity of a bond or similar cash flow stream rather than its legal maturity.

[2] Specific tax advice is beyond the scope of this whitepaper, and we highly recommend consulting with an expert when it comes to tax related questions. No specific tax advice is provided in this whitepaper. Family-specific structures require qualified counsel.

[3] A Section 1031 exchange, named for Internal Revenue Code (IRC) Section 1031, permits deferral of capital gains taxes on the sale of investment or business-use real property when proceeds are reinvested in like-kind replacement property of equal or greater value.

## Appendix

Consider a \$100 million ground lease investment on a new multifamily project with a total combined property value (CPV) of \$285.7 million. Land is allocated 35% of CPV (\$100 million) and improvements 65% (\$185.7 million).

Step 1 — Calculate initial annual rent.

- Initial yield = 5.00%
- Year 1 rent = 5.00% × \$100 million = \$5.00 million

Step 2 — Apply fixed escalator<sup>[1]</sup>.

- Year 10 rent = \$5.00 million × (1.02)<sup>9</sup> = \$5.98 million
- Year 30 rent = \$5.00 million × (1.02)<sup>29</sup> = \$9.08 million
- Year 50 rent = \$5.00 million × (1.02)<sup>49</sup> = \$13.80 million
- Year 99 rent = \$5.00 million × (1.02)<sup>98</sup> = \$34.76 million

Step 3 — Calculate cumulative undiscounted cash flow over the term. This is the future value of a growing annuity:

- Cumulative cash = \$5.00 million × [(1.02)<sup>99</sup> – 1] / 0.02 ≈ \$1,803 million

Step 4 — Estimate reversion value assuming total property appreciates at a conservative 2.75% annually<sup>[2]</sup>.

- Year 99 CPV = \$285.7 million × (1.0275)<sup>99</sup> ≈ \$1,420 million
- Assuming land remains ~35% of CPV at maturity, land value ≈ \$497 million.
- Improvement reversion to lessor ≈ \$923 million

Step 5 — Total undiscounted value created.

- Cumulative rent is \$1,803 million + reversion \$923 million = \$2,726 million on \$100 million invested, or 27.3× money over 99 years.

Even discounting intermediate cash flows and reversion at a 6.25% required IRR (typical for the asset class today), the transaction still generates an unlevered IRR of approximately 8.1%. Adding conservative 55% non-recourse leverage at SOFR + 225 bps pushes levered IRR to 12–14% with ground-lease-to-value remaining below 45%.

Assumptions:

- The above example uses modern, unsubordinated, 99-year, triple-net ground leases with institutional protections.
- Long-term appreciation 2.75% nominal; CPI 2.0–3.0%; tax rates reflect current law as of November 2025.

[1] Assumes 2.00% annual fixed increases, compounded.

[2] The long-term U.S. commercial real estate average per NCREIF.

# About the Author

Marc J. Sharpe is a global investment executive and board member with a distinguished career spanning family office management, private equity, venture capital, and investment banking. Known for his strategic insight, deep expertise in family office governance, and ability to foster innovation and value creation, Mr. Sharpe has built and led investment platforms that deliver sustainable growth while navigating complex financial and operational challenges. His leadership style emphasizes integrity, continuous improvement, and long-term partnerships that generate significant stakeholder value. Mr. Sharpe is the Founder and Chairman of The Family Office Association, a premier global peer network of single-family offices. Since 2007, he has cultivated a community of senior family office executives and principals representing some of the world's wealthiest families, promoting education, shared-best practices, and co-investment opportunities. Under his leadership, TFOA has become a trusted forum for collaboration, market insight, and proprietary investment deal flow on a global scale. He also teaches an MBA class on "The Entrepreneurial Family Office" as an Adjunct Professor at Rice University and Southern Methodist University. Mr. Sharpe holds an M.A. from Cambridge University, an M.Phil. from Oxford University, and an MBA from Harvard Business School.

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