Tax Policy

In 2017, Congress passed the most comprehensive and far-reaching changes to the tax code in more than a generation. Today, The Roundtable is working actively with policymakers to ensure that the Tax Cuts and Jobs Act is implemented smoothly and efficiently, in a way that reduces economic disruption and achieves Congress's reform objectives: capital formation, productive investment, and job creation.

The real estate industry is one of the leading job creators—employing more than one in every ten full-time U.S. workers—and taxes on real estate represent close to 70 percent of local tax revenues. The Tax Cuts and Jobs Act influences all aspects of real estate activity, including development, construction, ownership, and management. The positive effects of the tax changes already are evident in the economy. However, the final regulatory rules for new provisions, such as the 20 percent deduction for pass-through business income, will be critically important to the long-term success of the tax law. Smart and well-designed Treasury rulemaking and guidance will help real estate continue to drive economic activity and create jobs.

In 2019, The Roundtable tax policy agenda includes stimulating investment in distressed areas through the effective implementation of the Opportunity Zone program; removing barriers to outside investment in U.S. real estate and infrastructure through repeal of the Foreign Investment in Real Property Tax Act (FIRPTA); and ensuring that new Treasury regulations protect key elements of tax reform, such as the deductibility of business interest for commercial real estate. In addition, The Roundtable will work with lawmakers to enact important technical corrections and with stakeholders to preserve and sustain the Supreme Court's recent *Wayfair* decision, which promotes a level economic playing field by allowing States to impose sales tax collection requirements on internet retailers.

Sen. Tim Scott (R-SC), who serves on the Senate Banking, Housing and Urban Affairs; and Finance Committees, discusses the importance of Opportunity Zones for job growth and communities across the U.S. (Photo courtesy of Gage Skidmore)

Opportunity Zones—Boosting Real Estate Investment & Economic Development in Distressed Communities

The Tax Cuts and Jobs Act includes a new tax incentive aimed at spurring economic development and job creation in distressed areas. The tax incentives allow Qualified Opportunity Funds that make long-term investments in designated zones to reduce the burden of capital gains tax for their investors. The Roundtable provided comments to the Treasury Department last June detailing ways in which the program could attract capital, stimulate job-creating investment, and fulfill its objectives. Many of the Roundtable recommendations were included in October's proposed regulations.

Opportunity Zones offer enormous potential to channel investment and spur economic growth in low-income communities. Unlike previous attempts to use tax incentives to spur private investment in distressed areas, investors do not have to compete with one another for a limited number of tax credits in a costly, centralized process. Opportunity Zones also promote the pooling of capital through Opportunity Funds. This pooling could be transformative in mobilizing capital from disparate sources to support jobs and growth. Moreover, the fund structure that underlies the program may result in a business model where local entrepreneurs with knowledge and expertise partner with outside investors, creating a new cadre of business leaders and lasting benefits for the community.

Real estate investment is an economic multiplier and a catalyst for permanent, lasting job creation. The ability of Opportunity Zones to unlock private capital for real estate investment will be a principal determinant of the program's effectiveness. Final Opportunity Zone implementing guidance should seek to maximize the flow of real estate investment, capital, and jobs into the designated communities by providing greater clarity and comfort to potential investors regarding the types of activities and investments that qualify.

Eliminating Barriers to Foreign Investment in U.S. Real Estate and Infrastructure

The Roundtable supports the Invest in America Act, legislation introduced last September by Representatives Kenny Marchant (R-TX) and Joseph Crowley (D-NY) to repeal the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA). FIRPTA subjects foreign investment in US real property to a much higher tax burden than foreign investment in any other class of assets. Congress passed important FIRPTA reforms in 2015, including an exemption

Sen. Charles E. Schumer (D-NY), who serves as Minority Leader in the Senate, discusses the importance of international tax reform, and its potential impact on the commercial real estate industry with Roundtable members.

for foreign pension funds, but more is needed. FIRPTA effectively deters billions of dollars of capital that would strengthen US real estate and infrastructure, expand the tax base, and create well-paying domestic jobs. Its repeal would expand the availability of capital, improve market liquidity, and directly create jobs in construction, finance, and real-estate related industries, in addition to supporting industries that provide goods and services.

The Roundtable is also seeking administrative relief for inbound real estate and infrastructure investment through the repeal of IRS Notice 2007-55. The Notice improperly subjects the liquidating distributions of domestically controlled REITs to FIRPTA. In 2017, 32 Members of Congress wrote to Treasury Secretary Mnuchin noting the negative effect of the Notice on real estate investment and asking that he repeal it.

Tax Reform Implementation—Treasury Regulations and Technical Corrections

Qualified Improvement Property. The Roundtable is working to advance a much-needed technical correction to the Tax Cuts and Jobs Act that would fix a drafting error that has unintentionally pushed the cost recovery

Opportunity Zones: Promoting Economic Development Through Productive Real Estate Investment

8,762	35 Million	75%	50
Number of designated and certified Opportunity Zones	People in the US, including Puerto Rico, live in Opportunity Zones	Of Opportunity Zones are in zip codes that experienced at least some employment growth from 2011 to 2015	Median age in years of housing stock in the average Opportunity Zone, more than 10 years older than the U.S. median

Source: Economic Innovation Group (November, 2018)

period for qualified improvement property (QIP) from 15 to 39 years. QIP covers a broad category of improvements to the interior of nonresidential real estate, including leasehold improvements. Congress intended to allow the immediate expensing of qualified improvements, or provide a 20-year recovery period in the case of taxpayers electing out of new limitations on the deductibility of business interest. As a result of the mistake, some businesses across the country are delaying or significantly reducing capital expenditures for building improvements, undermining job creation and economic activity.

The QIP issue could be addressed through technical corrections legislation or administrative guidance from the Treasury Department. "In 2015, Congress voted overwhelmingly to permanently extend the 15–year recovery period for certain property improvements. By passing tax reform, Congress intended to consolidate those changes. Treasury should now use its authority to provide taxpayers with relief until a technical corrections bill is enacted. Treasury guidance will remove taxpayer uncertainty, unlock investment, and spur job-creating property upgrades and renovations."

20% Pass-through Business Deduction. The Tax Cuts and Jobs Act reduced the top tax rate on corporations from 35% to 21%, but also included a new 20% pass-through deduction (section 199A) that can lower the top tax rate on qualifying pass-through business income to 29.6%. Such income was previously taxed at a top rate of 39.6%. The Roundtable has offered several suggestions to the Treasury to maximize the economic benefits of the pass-through deduction and avoid unnecessary restructuring costs or disruptions to business activity. For example, final section 199A regulations should allow real estate owners to aggregate properties and entities when calculating their deduction, and should not penalize taxpayers for participating in a like-kind exchange transaction. The Roundtable is committed to ensuring that the new tax law treats all types of business, including real estate, fairly and equitably.

Limitation on the Deductibility of Business Interest. Tax reform also included rules that allow real estate businesses to continue fully deducting interest related to business debt. The exception for interest allocable to a real property trade or business reflects policymakers' understanding that limits on the deduction for interest expense could have severe negative consequences for property values, real estate markets, and economic growth. Final Treasury regulations should clarify that interest (other than investment interest) on debt that is allocable to an owner of an entity engaged in a real property trade or business is exempt from the new business interest limitation rule—if that trade or business has elected out of the rule.

As Treasury and Congress continue to focus on implementation and corrections to the new tax law, The Roundtable and TPAC will continue to play an active role in seeking appropriate clarifications affecting the most significant changes to the tax code.

Working with Policymakers to Implement *Wayfair*

Last June, the Supreme Court ruled in *South Dakota v. Wayfair* to expand states' authority to collect sales and use taxes on internet consumer purchases from retailers who do not have a physical presence in the state. The Roundtable submitted amici briefs in support of South Dakota at various stages of the litigation. The *Wayfair* decision will enable states to collect much-needed revenue to provide public services and invest in local infrastructure projects. The decision marks a monumental step forward in the effort to create a level playing field between internet retailers and Main Street stores.

In September, The Roundtable and seven other national trade organizations wrote to congressional leaders to oppose legislation that would reverse or limit the Supreme Court's decision. The proposed legislation would have barred states from collecting taxes from out-of-state internet vendors until 2019. It would have prohibited states from requiring remote sellers with less than $10 million in national annual sales to collect and remit sales and use taxes, pending a "simplification compact" that Congress would have to approve. Legislation hastily enacted post-ruling could create unnecessary uncertainty and complicate states' implementation of *Wayfair*.

The Roundtable supports a level playing field between online and brick-and-mortar sellers that reflects the changing dynamics of today's omnichannel marketplace. We remain committed to working with Congress on any problems that may arise from state implementation of remote internet sales tax collection allowed by *Wayfair*.

Tax Policy in a Divided Congress

The tax policy landscape will change dramatically in 2019 as control of the House of Representatives shifts to Congressional Democrats. The new Majority in the House will seek to leave its own imprint on tax and economic policy. As Congress reexamines recent legislation, including the Tax Cuts and Jobs Act, The Roundtable will continue to work with lawmakers to raise awareness of how elements of the tax law encourage capital formation, reflect the economics of real estate assets and entities, and contribute to strong property values and well-served, livable communities.