04

Tax Policy
The Roundtable advocates for tax policies that facilitate capital formation, reward risk-taking, and bolster productive private investment.

Over the past year, these tax policy objectives were challenged on a number of fronts as lawmakers and the Administration looked for new revenue sources to pay for ambitious legislative proposals. Despite these challenges, The Roundtable continued to provide policymakers with fact-based, credible research on the benefits of preserving longstanding tax treatments. The Roundtable has been an active member of multiple coalitions of industry leaders and stakeholder organizations educating Congress and the Administration on the importance of a competitive tax system. Moreover, The Roundtable continues to be a staunch proponent of expanding tax provisions and incentives that contribute to job creation and economic growth—such as Opportunity Zones (OZs) and the Low-Income Housing Tax Credit (LIHTC).

President Biden’s Budget & BBB Tax Issues

Democrats in Congress and the Administration have negotiated sporadically throughout the last year over which climate and social spending priorities would be included as part of an overall Build Back Better (BBB) reconciliation package and how those proposals would be paid for. Proposed or considered tax increases include those that would affect partnerships and pass-throughs, unrealized appreciation, the transfer of assets at death, like-kind exchanges, carried interest, and capital gains, among others.

Several of these proposed pay-fors in the House of Representatives-passed BBB and the Administration’s recent budget request to Congress would directly increase the tax burden on real estate investment and consequently hurt property values, local government budgets, and real estate’s ability to continue supporting communities, jobs, and economic growth.

Beginning early in the process, The Roundtable, along with 16 other national real estate trade organizations, submitted detailed comments to Congress arguing against the inclusion of tax proposals that would have unintended consequences on the real estate industry and the overall economy. During the height of these discussions, The Roundtable held an all-member town hall in August 2021 with Rep. Tom Suozzi (D-NY), a member of the tax-writing House Ways and Means Committee, to discuss these and other issues and make the position of the industry clear to congressional leaders.

In September, The Roundtable and a broad coalition of leading organizations representing millions of individually- and family-owned businesses urged members of Congress to reject proposed tax increases on pass-through businesses, including a cap on the pass-through business income deduction (section 199A). Widely distributed Roundtable modeling of the initial House Ways and Means Committee bill demonstrated the disproportionate tax burden that would fall on pass-through businesses vis-à-vis public corporations.

In October, The Roundtable joined other organizations in encouraging lawmakers to preserve longstanding grantor trust and valuation rules in any BBB package.
Our advocacy efforts helped avoid the inclusion of several potential tax increases that would be detrimental to real estate and its contribution to the economy. Notably, and in stark contrast to the first version of the legislation, the November House-passed BBB Act included:

- No limit to like-kind exchanges (sec. 1031),
- No increase in the capital gains tax rate,
- No restrictions on the 20% pass-through business income deduction (sec. 199A),
- No tax on unrealized gains at death or repeal of the step-up in basis of assets,
- No change in the tax treatment of carried interest,
- No change in grantor trust and valuation rules, and
- No restriction of estate tax valuation discounts.

The Roundtable’s Tax Policy Advisory Committee (TPAC) and staff work closely with the congressional tax-writing committees to ensure lawmakers understand and appreciate the potential unintended consequences of tax increases on the real estate industry and a growing, yet fragile, economy.

**Capital Gains**

Capital formation is key to a strong financial system and modern economy. By rewarding risk and encouraging investment, a meaningful capital gains incentive directly drives economic growth and job creation.

Historically, the U.S. has taxed capital gains at a lower rate than ordinary income; however, the president and several members of Congress have proposed raising the rate from 20% to 39.6%. The president would also expand the scope of the separate 3.8% net investment income tax to cover a broader share of real estate investments and eliminate the special 25% rate that applies to gains attributable to prior depreciation deductions (depreciation recapture). The advocacy efforts of The Roundtable and others were successful in dissuading Congress from including an increase in the capital gains rate as part of the 2021 House-passed BBB Act.

The administration’s recent FY2023 budget also proposes to tax the wealthiest households on their unrealized capital gains, including real estate. It would impose a minimum levy of 20% on a comprehensive tax base that includes both realized income and unrealized annual appreciation of a taxpayer’s assets. Some members of Congress, such as Senate Finance Chairman Ron Wyden (D-OR), would go even further, taxing the unrealized gains of taxpayers with $10 million or more in assets.

Taxing unrealized gains would upend over 100 years of federal taxation, require an unprecedented IRS intrusion into household finances, and create unknown and unintended consequences for the U.S. economy.

A reduced rate on capital gains decreases the cost of capital, drives long-term investment, encourages productive entrepreneurial activity, draws investment from around the world, and increases U.S. workforce productivity and competitiveness. The Roundtable is committed to preserving a meaningfully reduced tax rate on capital gains (relative to ordinary income) that continues to apply only when gains are realized.

**Step-Up In Basis**

When an individual dies, the U.S. levies a comprehensive tax on his or her wealth and assets, including unrealized gains, through the estate tax where wealth that exceeds an exemption amount ($6 million in 2022) generally is taxed at a rate of 40%. Separately, for income tax purposes, the basis of assets in the hands of an heir is “stepped up” to fair market value at the time of the decedent’s death. President Biden and some lawmakers have proposed adding a second layer of tax at death, on top of the estate tax, by imposing a capital gains income
tax of 39.6% on a decedent’s unrealized gains, effectively repealing current law’s step-up in basis.

Applying capital gains tax to appreciated property at the same time that the tax code is applying a 40% estate tax to the asset’s full fair market value is punitive and confiscatory and would force many family-owned and closely held real estate businesses to liquidate rather than grow and continue from one generation to the next.

In 2021, The Roundtable and other members of the Family Business Estate Tax Coalition commissioned EY’s Dr. Bob Carroll, the former Deputy Assistant Secretary of Treasury for Tax Analysis, to evaluate the economic consequences of eliminating step-up in basis. The report concluded that if step-up in basis were repealed, 40,000 jobs would be lost every year in the first 10 years after enactment, and GDP would decrease by $50 billion over 10 years.

The coalition’s report and sustained, coordinated advocacy, including letters to key lawmakers, played a central role in persuading the congressional majority to retain longstanding tax rules that apply to assets transferred at death in the House-passed BBB Act.

**Impact of Repealing Step-Up in Basis**

- **40,000 jobs** would be lost every year in the first 10 years since enactment
- GDP would decrease by **$50 billion over 10 years**

*Source: Ernst & Young, Repealing Step-Up of Basis on Inherited Assets: Macroeconomic Impacts and Effects on Illustrative Family Businesses, April 2021*

**Pass-Through Business Income**

Closely-held partnerships and pass-through businesses allow income to pass through to individual owners rather than taxing the income at the entity level, giving owners flexibility in how they structure the risks and rewards of the business. Pass-through regimes are a strength of the U.S. tax system and contribute to the American entrepreneurial culture and a competitive and dynamic economy.

In 2017, Congress reduced the corporate tax rate by 40% and also created a new 20% deduction (section 199A) for pass-through business income to avoid putting businesses organized as partnerships, S corporations (S corps), and real estate investment trusts (REITs) at a competitive advantage relative to large C corporations (C corps). However, in July 2021, Senator Ron Wyden (D-OR), chairman of the Senate Finance Committee, proposed repealing the 20% deduction for pass-through business income for taxpayers earning over $400,000/
year. Not long thereafter, legislation passed the House Ways and Means Committee that would have capped the maximum deduction at no more than $500,000.

Section 199A provided critical tax relief to the nearly 40% of individually- and family-owned businesses that were forced to shut their doors during the COVID-19 pandemic. Congress’ proposed changes would have contributed to raising the top marginal tax rate on the owners of small, private, and closely held businesses from 29.6% to 46.4%.

While the proposed tax increases were reduced in the House-passed BBB Act, Senator Wyden has circulated multiple discussion drafts of legislation that would increase the tax burden on partnerships and pass-through businesses. His proposals would reduce flexibility in how partnerships are formed, how property is contributed, and how debt and income are allocated to partners.

The Roundtable has taken a leading role in coordinating advocacy, comments, and input from the real estate industry on potential changes to partnership taxation, emphasizing that Congress should focus on reforms that will strengthen and expand partnerships’ ability to create jobs and economic opportunities while avoiding proposals that discriminate against specific industries.

Nearly 2 million U.S. partnerships with more than 8 million partners are engaged in leasing and other real estate-related activities, such as brokerage and construction.
Like-Kind Exchanges (LKEs)

Since 1921, the tax code has encouraged taxpayers to reinvest and grow their businesses by deferring capital gains when exchanging real property used in a trade or business for property of a like-kind (section 1031). We estimate that close to 20% of all commercial real estate transactions involve an LKE. Exchanges were preserved in the Tax Cuts and Jobs Act, and The Roundtable believes they should be retained in any future tax reform efforts.

Led by The Roundtable and other stakeholders, the broad-based Real Estate Like-Kind Exchange Coalition has sponsored critical academic and outside research on LKEs and their economic impact.

The studies have found that LKEs:

- Increase net investment
- Boost tax revenue
- Stimulate capital expenditures leading to job growth
- Reduce leverage and financial risk
- Lower rents for households
- Support healthy property values

In short, like-kind exchanges are fundamental to the health and financing of commercial real estate; they spur capital investment, particularly during market corrections and liquidity shortages.

The coalition has also sponsored bipartisan briefings for congressional staff, submitted testimony, and written detailed letters to lawmakers on the benefits of LKEs.

Economic Activity Supported by the Like-Kind Exchange Rules in 2021

- **976K** total jobs supported by like-kind exchange rules
- **$48.6B** total labor income supported by like-kind exchange rules
- **$13B** total federal, state, and local taxes supported by like-kind exchange rules

Source: Ernst & Young, Economic Contribution of the Like-Kind Exchange Rules to the US Economy in 2021: An Update, May 2022
Carried Interest

Carried interest is the interest in partnership profits a general partner receives from the investing partners for managing the investment and bearing the entrepreneurial risk of the venture. Carried interest may be taxed as ordinary income or capital gain depending on the character of the income generated by the partnership. Even as changes to carried interest tax rules were dropped from the final House-passed BBB Act, recent proposals by President Biden and others would convert all carried interest income attributable to gain from the sale of real estate to ordinary income.

These proposals would make it more expensive to build or improve real estate and infrastructure, including workforce housing, assisted living communities, industrial properties, and more. Some development simply won’t happen, especially in long-neglected neighborhoods or on land with potential environmental contamination.

Our tax code should reward risk-taking. The Roundtable and other national real estate organizations have consistently made this clear to policymakers, articulating in letters to Congress the many economic benefits of preserving longstanding tax laws on carried interest, countering false narratives, and highlighting the potentially enormous consequences of raising taxes and discouraging entrepreneurial innovation, risk-taking, and sweat equity.

---

**Long-Run Economic Impact of Carried Interest Legislation**

<table>
<thead>
<tr>
<th>Real Estate-Related Job Losses</th>
<th>1.77 Million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reduction in Federal Tax Revenue</td>
<td>$11.22 Billion</td>
</tr>
<tr>
<td>Reduction in State/Local Tax Revenue</td>
<td>$26.74 Billion</td>
</tr>
</tbody>
</table>

*Source: Center for Capital Markets Competitiveness, Impact on Jobs, Tax Revenue, And Economic Growth of Proposed Tax Increase on Carried Interest, 2021*
Affordable Housing Tax Incentives

The low-income housing tax credit (LIHTC) is an innovative federal policy tool that has proven effective in stimulating the construction and rehabilitation of affordable housing. The market-based credit relies on the private sector to finance, build, and operate affordable housing by subsidizing a significant share of the construction costs as long as the owner agrees to maintain reduced rents. Since its inception, the LIHTC has financed the development of nearly 3.5 million affordable rental homes that house over 8 million low-income households.

Both the House-passed BBB Act and President Biden’s 2023 budget included significant proposed expansions of the LIHTC. The Roundtable applauds these efforts and will continue working with Congress to expand and grow the supply of affordable and workforce housing by investing greater resources in time-tested tax incentives such as the LIHTC.

Opportunity Zones

Created in 2017, Opportunity Zones (OZs) are designated, low-income census tracts where qualifying investments are eligible for reduced capital gains taxes. By channeling investment where it is needed most and prioritized by states and local communities, OZs help stimulate job creation and economic growth in low-income communities. In the short time since enactment, OZs have created jobs and spurred billions of dollars in new investment in economically struggling communities.

The Roundtable worked closely with Members of Congress and the Treasury Department to ensure that OZ implementing regulations would facilitate the program’s success. In addition, The Roundtable has encouraged Congress to consider further OZ legislation that would spur greater investment and capital formation, ensure the program’s longevity and impact, and bolster job growth in economically disadvantaged communities.

These advocacy efforts have contributed to the introduction of new bipartisan, bicameral legislation to update and amend the OZ incentives. The Opportunity Zones Transparency, Extension, and Improvement Act would:

- Extend expired OZ benefits,
- Sunset certain high-income census tracts, and
- Apply additional information reporting requirements to Opportunity Funds and their investors.

The legislation includes a Roundtable-requested, 2-year extension of the initial capital gains deferral period for prior gain that is rolled into an opportunity fund by an investor.

---

The Roundtable strongly supports innovative, proactive policy incentives like OZs that encourage risk-taking and help drive capital and economic opportunity to the country’s most distressed communities.
Opportunity Zone Impact

In 2020, the Council of Economic Advisors estimated that Opportunity Funds had raised

$75 billion

in private capital in the first two years

following the incentives’ enactment, including

$52 billion

that would not have otherwise been directed to these communities.

The Council projected this capital could lift

1 million

people out of poverty and decrease poverty in Opportunity Zones by 11%.

In addition to The Roundtable’s work on each of the above issues, The Roundtable has also advocated for legislation that will modernize outdated tax accounting rules that discriminate against condominium construction by imposing tax liability on developers during the construction period when units are being pre-sold to potential buyers. Bipartisan legislation, the Fair Accounting for Condominium Construction Act, would fix these rules, reduce the cost of building new housing, and help expand the nation’s housing supply, particularly in high-population, high-density areas.

The Roundtable has also supported changes to antiquated tax rules that limit the ability of real estate investment trusts (REITs) and real estate businesses to invest in their tenants, including retail tenants, at a time when there is a significant and urgent need for such investment to prevent job losses and bankruptcies in the retail sector and its supply chain. The Retail Revitalization Act would unlock capital for productive investment and promote a market-based solution where economic stress is widespread.

Lastly, The Roundtable is exploring tax policy options to encourage the conversion of existing properties, such as office and retail, to new and potentially more productive uses, including the provision of affordable and attainable housing.