Preserving Business Property Tax Deductions

Issue

Congressional Republicans are working to identify additional revenue offsets to finance a growing list of tax priorities. Tax-writers are considering limitations on the federal tax deduction for state and local taxes paid by businesses as a source of new revenue. These restrictions could take several forms. A cap on the deductibility of business-related property taxes would have devastating consequences for commercial real estate values, rents and the entire economy and financial system.

The 2017 Tax Cuts and Jobs Act (TCJA) imposed a $10,000 cap on the deductibility of state and local income and property taxes paid by individuals. The bill retained the deductibility of state and local business taxes ("Business SALT"), including: property taxes on business property (property used in a trade or business, or property held for investment), state corporate income taxes and state income taxes paid at the entity-level (state pass-through "work around" regimes). Business SALT restrictions are considered a potential offset for individual SALT relief, an extension of already-expired business provisions (e.g., bonus depreciation) or a further reduction of the corporate rate.

Advocates of limiting the deductibility of Business SALT offer two policy arguments. Some suggest, as a matter of tax parity, that businesses should be treated the same as individuals. Second, some argue that restricting the Business SALT deduction would put pressure on states to further lower their tax burden on job creators. Most importantly, according to modeling by Penn-Wharton and the Tax Foundation, repealing the deductibility of Business SALT could raise over $1 trillion over 10 years:

- Repeal deductibility of corporate income taxes: $290B/10 years
- Repeal deductibility of business property taxes: $503B/10 years
- Disallow state pass-through workarounds: $210B/10 years

The Roundtable's Position

Repealing the deductibility of state and local business property taxes would cause unimaginable damage to U.S. commercial real estate, local communities and the broader economy and must be avoided.

- State and local property taxes represent 40 percent of the operating costs of U.S. commercial real estate. Property taxes are a greater expense than utilities, maintenance and insurance costs combined.
- Business-related property taxes are different from state and local income taxes. Property taxes are an unavoidable expense, an inescapable cost of operating any business. They are a cash outlay that is owed regardless of whether the business has any income at all.
- Eliminating or capping this deduction could:
    - **Raise effective tax rates to 1970s-era levels near 50 percent**, discouraging investment in housing, infrastructure and economic development projects nationwide. This would reverse the benefits of the TCJA and Section 199A.

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- **Raise business owners' property tax bills in effect by roughly 40 percent**, causing employers to owe federal tax on money that they do not have. Real estate values will fall as investors rush to exit the market. Foreclosures, insolvencies and massive layoffs will result. New investment will dry up and badly needed housing will not be built.
- **Hit lower-rent housing the hardest**, drive up operating costs and deter construction at a time when housing affordability is already at a crisis point. The cost will be passed through to tenants as landlords are forced to raise rents. Lower-income renters will be the hardest hit because property taxes are a larger percentage of the total cost for these properties.
- **Stall housing development**, erode property values and undercut local tax bases that fund schools, fire departments and more. Schools, police and other services will suffer as local tax revenue declines.
- Analysis by the Tax Foundation indicates that disallowing corporate SALT deductions for corporate income and property taxes would reduce GDP and American incomes by 0.6 percent and reduce hours worked by 147,000 full-time equivalent jobs.

Additional Resources

- Roundtable Weekly, "Real Estate Industry Fights to Preserve Business Property Tax Deductions Amid GOP Tax Negotiations" (March 17, 2025)
- Roundtable Weekly, "Real Estate Industry Urges Congress to Preserve Deductibility of Business Property Taxes" (March 7, 2025)
- RER letter, "Preserve the Full Deductibility of Business-Related Property Taxes" (March 7, 2025)

Pass-Through Business Income

Issue

Real estate generally is owned and operated through "pass-through" entities. In 2017, Congress reduced the corporate tax rate by 40 percent and created a new 20 percent deduction (section 199A) for pass-through business income to avoid putting partnerships, S corporations and REITs at a competitive advantage relative to large C corporations.

Section 199A expires at the end of 2025. At that time, the effective marginal rate on pass-through business income would rise by over one-third, from 29.6 percent to 39.6 percent.

Tax legislation considered in 2021 would have raised the top marginal income tax rate on many small and pass-through business owners from 29.6 percent today to 46.4 percent.

The Trump administration supports extending all of the expiring 2017 tax cuts, including section 199A.

The Roundtable's Position

Congress should continue to support closely-held, entrepreneurial businesses that create jobs and spur growth, and reject tax changes that discriminate against pass-through entities.

- Our pass-through regime is a competitive strength of the U.S. tax system. Most countries rely on inflexible corporate regimes that provide little ability for an entrepreneur to tailor the capital and ownership structure to meet the needs of the business and its investors.
- Small and closely-held businesses drive job growth and entrepreneurial activity in the United States. Entity choice is a differentiator that contributes to our entrepreneurial culture.
- Half of the 4 million partnerships in the U.S. are real estate partnerships, and real estate activity constitutes a large share of pass-through business activity.
- Listed REITs allow small investors to invest in diversified, commercial real estate using the same single tax system available to partners and partnerships.
- Partnerships, Limited Liability Companies (LLCs), S corps and REITs are ideal for real estate because they give investors flexibility in how they structure the risks and rewards of these capital-intensive and relatively illiquid businesses.
- Any new tax legislation should avoid the unintended consequences and potential harm caused by the stacking of tax increases on pass-through entities.
- Section 199A is appropriately targeted at businesses that hire workers and invest in capital equipment and property.
- Section 199A also helps preserve tax fairness vis-à-vis large corporations.

Carried Interest

Issue

A "carried" interest is the interest in partnership profits that a general partner receives from the investing partners for managing the investment and taking on 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. Lawmakers have introduced various proposals to increase the tax burden on carried interest since 2007. In 2017, Congress created a three-year holding period requirement for the reduced long-term capital gains rate.

In February, President Trump informed Republican congressional leaders that one of his main tax priorities this year is "closing the carried interest tax deduction loophole." Shortly thereafter, a group of 13 Senate Democrats reintroduced the Carried Interest Fairness Act (S. 445). The bill would convert virtually all real estate-related carried interest income to ordinary income subject to the top tax rates and self-employment taxes.

During his first term in office, President Trump reportedly pushed Republican lawmakers to include much stricter restrictions on carried interest than the three-year holding period that was included in the final 2017 tax bill.

In 2021, House Ways and Means Democrats passed legislation to extend the carried interest holding period from three to five years, and other changes, while adding a new exception for a real property trade or business (e.g., real estate). The proposals were not enacted.

Former Senate Finance Chairman Ron Wyden (D-OR) has proposed treating carried interest as an interest-free loan from the limited partners to the general partner that is taxable upon grant, regardless of whether the partnership ever generates any profits.

The Roundtable's Position

- The tax code should reward risk-taking; the capital gains rate should apply to more than just invested cash.
- Carried interest changes would harm small businesses, stifle entrepreneurs and sweat equity and threaten future improvements and infrastructure in neglected areas. They would increase the cost of building or improving infrastructure, workforce housing and assisted living, and deter risky projects, such as sites with potential environmental contamination.
- Carried interest is not compensation for services. General partners receive fees for routine services (leasing, property management). Those fees are taxed at ordinary tax rates.
- Carried interest is granted for the value the general partner adds beyond routine services, such as business acumen, experience and relationships. It is also a recognition of the risks the general partner takes with respect to the general partnership's liabilities (funding pre-development costs, guaranteeing construction budgets, potential litigation).
- Carried interest proposals apply retroactively to prior transactions and partnership agreements executed years earlier. The agreements were based on tax law as it existed at the time. By changing the results years later, they would undermine the predictability of the tax system and discourage long-term, patient investment.

Carried Interest

Additional Resources

- RER letter, "Avoid New Tax Hikes on America's Real Estate" (March 26, 2025)
- Roundtable Weekly, "Real Estate Challenges: Business SALT, Carried Interest Emerge as Focal Points of Tax and Budget Discussions" (February 21, 2025)
- Roundtable Weekly, "Tax Policy This Week in Washington: Carried Interest and Budget Talks" (February 7, 2025)

Opportunity Zones

Issue

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, OZs help stimulate jobs and growth in low-income communities.

The three main OZ tax benefits were a deferral of prior capital gain rolled into an OZ fund, an increase (partial "step-up") in the basis of the prior investment after a five or seven-year holding period and the exclusion of gain on the OZ investment after 10 years.

The final OZ regulations were issued four months before the COVID-19 lockdown. The tax benefits are gradually phasing down (the deferral of prior gain ends in 2026) and the partial basis step-up has expired for new OZ fund contributions.

In the last Congress, bipartisan House legislation (Reps. Mike Kelly, R-PA and Dan Kildee, D-MI; H.R. 5761) would extend OZ deadlines for two years, allow helpful "fund of funds" OZ tax structures, sunset certain high-income OZ census tracts and create new OZ information reporting and transparency rules.

The renewal and reform of the OZ tax incentives is expected to be a major topic of discussion as Congress considers extension of the 2017 tax bill in 2025.

The Roundtable's Position

- In their short tenure, OZs have created jobs and spurred billions of dollars in new investment in economically struggling communities across the country.
- Opportunity Funds finance affordable, workforce and senior housing; grocery-anchored retail centers; and commercial buildings that create spaces for new businesses and jobs.
- In 2020, the White House Council of Economic Advisors estimated that the Opportunity Funds had raised $75 billion in private capital in the first two years following the incentives' enactment, including $52 billion that otherwise would not have been raised. The council projected this capital could lift one million people out of poverty in OZs by 11 percent.
- The decentralized design of OZs allows more investors and stakeholders to participate in the market and invest in qualifying projects that generate economic opportunity and improve the built environment in high-need communities.
- Congress should ensure that OZs continue to act as a catalyst for economic development in struggling communities by passing legislation that extends OZ deadlines.
- Congress should also continue working on improvements to the OZ tax incentives, such as enhanced information reporting, data collection and transparency, as well as lowering the substantial improvement threshold to cover a broad range of real estate rehabilitation and redevelopment projects.

Tax Policy

Preferential Rate and Realization Requirement

Issue

Traditionally, the United States has taxed long-term capital gain at a lower rate than ordinary income. The only exception was a brief three-year period after the Tax Reform Act of 1986 when Congress lowered the top ordinary tax rate from 50 percent to 28 percent and created temporary tax parity between ordinary and capital income. Long-term capital gain is currently taxed at a top rate of 20 percent. However, the rate increases to 23.8 percent if the income is subject to the 3.8 percent tax on net investment income. The net investment income tax applies to real estate gains earned by passive investors and not income earned from the active conduct of professionals in real estate.

The prior Biden administration proposed raising the capital gains rate to 39.6 percent, which would bring it to parity with its proposed top rate on ordinary income. In addition, former President Biden had proposed to increase the 3.8 percent tax on net investment income to 5 percent and extend it to the income of active business owners, including real estate professionals; the net investment income tax applies to both capital gains and rental income.

Former President Biden and several key Democratic lawmakers have also previously proposed a mark-to-market regime in which built-in, unrealized gain is taxed on an annual basis, regardless of whether the asset is sold.

The Roundtable's Position

Congress should continue to encourage investment and job creation with a meaningful capital gains incentive.

- Maintaining a reduced tax rate on capital gain 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.
- Policymakers should reward risk-taking and investment in communities where it is needed, not punish it.
- High taxes on capital income make it harder to attract the investment needed to rebuild our urban centers. Opportunity Zone capital gains incentives facilitated $75 billion in new investment in low-income communities in the first two years after enactment.
- Risk capital differs from wage compensation. The entrepreneur who foregoes a traditional job in favor of starting a business forfeits many protections and benefits offered to employees, such as a pre-negotiated salary. The capital gains preference compensates entrepreneurs for this risk, including the potential complete loss of their time and capital.
- The reduced capital gains rate partially offsets the higher risk with illiquid, capital-intensive real estate projects, as well as the economic effects of inflation.
- Unlike other tax policies, such as immediate expensing, the capital gains preference only rewards smart, productive investments that generate profits.
- A tax on unrealized gains would require the IRS to police households as they identify, tabulate and value all their worldly possessions. The tax would thrust the IRS into a new and unwelcome role. The agency would become a permanent, live-in accountant and watchdog over every aspect of household's finances, consumer activity and economic life.

Preferential Rate and Realization Requirement

- In addition, taxing unrealized gains would trigger wasteful disputes and litigation, detracting from productive economic activity. Annual valuation requirements will require costly appraisals. Valuation disagreements will be a constant source of audits and administrative appeals.
- Current law encourages taxpayers to put capital to work on projects that won't pay off for many years. By taxing business assets and investments annually, a tax on unrealized gains would remove one of the major incentives for patient, productive capital investment. The differential tax treatment of liquid and illiquid investments will distort markets and give rise to wasteful new tax shelters and taxpayer games.
- A proposed tax on unrealized gains is quite possibly unconstitutional. Supreme Court jurisprudence has applied a realization requirement to determine whether gains or profits constitute income taxable under the 16th Amendment. Since the proposed tax applies to both realized and unrealized gains, it may go beyond the boundaries of Congress's taxing power.

Real Estate Like-Kind Exchanges

Issue

Since 1921, the tax code has allowed taxpayers to defer capital gain when exchanging real property used in a trade or business for a property of a like-kind (section 1031). In 2017, Congress narrowed section 1031 by disallowing its use for personal property (art, collectibles, etc.).

The prior Biden administration would have restricted gains deferred through like-kind exchanges to no more than $500K per year ($1M/couple). A similar proposal has appeared in the last six budgets submitted by Democratic administrations.

The Roundtable's Position

Congress should support healthy real estate markets and property values by preserving the current tax treatment of like-kind exchanges.

- 15-20 percent of commercial transactions involve a like-kind exchange. Exchanges get languishing properties into the hands of new owners who improve them and put them to their best use.
- Like-kind exchanges helped stabilize property markets at the height of the COVID-19 lockdown. Exchanges are even more important during periods of market stress when external financing is harder to obtain. Section 1031 is facilitating a smoother transition as real estate assets are re-purposed in the post-COVID economy.
- Like-kind exchanges allow businesses to grow organically with less unsustainable debt, creating a ladder of economic opportunity for minority-, veteran- and women-owned businesses and cash-poor entrepreneurs that lack access to traditional financing.
- Academic and outside research has found that exchanges spur capital expenditures, increase investment, create jobs for skilled tradesmen and others, reduce unnecessary economic risk, lower rents and support property values.
- Roughly 40 percent of like-kind exchanges involve rental housing. Section 1031 helps fill gaps in the financing of affordable housing. Unlike the low-income housing tax credit, developers can use section 1031 to finance land acquisition costs for new affordable housing projects.
- Exchanges help low-income, hard-hit and distressed communities where outside sources of capital are less available. Section 1031 also supports public services (police, education) by boosting transfer/recording/property taxes (nearly 3/4 of all local tax revenue).
- Land conservation organizations rely on exchanges to preserve open spaces for public use or environmental protection.
- Section 1031 is consistent with corporate and partnership tax rules that defer gains when the proceeds are retained and reinvested in businesses (sections 721, 731, 351, and 368).

Tax Policy

Business Interest Deductibility

Issue

The 2017 tax bill included strict new limits on the deductibility of business interest but also included a key provision that allows commercial real estate (a real property trade or business) to opt out of the interest limitation. The original House Republican tax plan—the House blueprint for tax reform—would have eliminated the deductibility of all business interest (including commercial real estate debt) while replacing depreciation rules with the immediate expensing of all future capital investment, including real property.

The final legislation included a revised section 163(j) in which the deductibility of business interest is generally limited to 30 percent of the taxpayer's EBITDA (earnings before interest, tax, depreciation and amortization). It also included 100 percent expensing of equipment and machinery (not real estate) for five years, phasing down thereafter. The 30 percent interest limit does not apply to an electing real estate business. However, an electing real estate business is required to use the alternative depreciation system, which includes slightly longer cost recovery periods for real property and cannot immediately expense leasehold and other interior improvements.

Since 2022, the general 30 percent business interest limitation has applied a less favorable rule that uses the taxpayer's EBIT (earnings before interest and tax) rather than EBITDA as the base for measuring the amount of deductible interest.

In 2025, extension of EBITDA rule, which was in effect from 2018-2021, is under review as Congress considers extension of the 2017 tax bill.

The Roundtable's Position

- Debt is a fundamental part of a real estate entity's capital structure and, in addition to property acquisition costs, is used to finance day-to-day operations like meeting payroll, buying raw materials, making capital expenditures and building new facilities.
- New restrictions on interest deductibility would cause enormous damage to U.S. commercial real estate by dragging down property values and discouraging new investment. Fewer loans could be refinanced, fewer projects could be developed, and fewer jobs would be created. Congress should extend the EBITDA rule that was in effect from 2018-2021.
- The ability to finance investment and entrepreneurial activity with borrowed capital has driven jobs and growth in the United States for generations. America's capital markets are the deepest in the world and provide our economy with a valuable competitive advantage.
- Business interest expense is appropriately deducted under the basic principle that interest is an ordinary and necessary business expense. Interest income is taxable to the recipient.
- Commercial banks are the dominant source of financing for commercial real estate investment. Like other entrepreneurs, small and medium-sized real estate developers and investors lack access to equity markets and rely on traditional lending to grow and expand.

Protecting Access to Foreign Investment in U.S. Real Estate

Issue

In April 2024, the Treasury Department issued final regulations under the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) that introduced a sweeping new "look-through" rule to determine whether a real estate investment trust (REIT) or regulated investment company (RIC) qualifies as a "domestically controlled qualified investment entity" (DCQIE) under Section 897(h)(4)(B) of the Internal Revenue Code.

Under FIRPTA, foreign investors are generally subject to U.S. capital gains tax on sales of U.S. real estate and most REIT shares—unlike gains on other U.S. investments. However, an exemption exists for domestically controlled REITs, where less than 50 percent of the shares are held "directly or indirectly" by foreign persons.

For decades, Treasury regulations interpreted the phrase "directly or indirectly" to refer to actual ownership and not constructive ownership through unrelated entities. Domestic C corporations—including those with significant foreign ownership—were treated as U.S. persons for purposes of determining whether a REIT was domestically controlled.

The 2024 final regulation reverses this position. It requires "look-through" treatment of any non-public domestic C corporation if 50 percent or more of its stock is held (directly or indirectly) by foreign persons. In such cases, the REIT shares held by the domestic C corporation are attributed up to its shareholders and counted as foreign-owned. The rule applies retroactively, including to long-established structures created under the prior legal regime.

At the state level, 20 states have enacted restrictions on foreign investors in real estate and agricultural land and eight states have considered similar measures.

- The Florida legislature enacted Senate Bill 264 in 2023, which aims to limit and regulate the sale and purchase of certain Florida real property by "Foreign Principals" from "Foreign Countries of Concern."
- The state-level restrictions have national implications and seem to fly in the face of the commerce clause of the Constitution in that they interfere with the free flow of interstate and foreign commerce.
- These foreign investment restrictions aim to safeguard national security but risk discouraging essential foreign capital crucial for refinancing and sustaining U.S. commercial real estate markets, particularly given upcoming debt maturities.
- RER urges careful implementation of these rules to prevent unintended consequences that could hinder economic growth and capital formation.

The Roundtable's Position

The FIRPTA look-through rule is legally unsound, economically harmful and inconsistent with congressional intent. Treasury should withdraw the rule and restore a stable, predictable framework for foreign investment in U.S. real estate.

Protecting Access to Foreign Investment in U.S. Real Estate

- **The rule exceeds Treasury's authority.** Congress explicitly authorized look-through rules for REITs and RICs in Section 897(h)(4)(E) but deliberately excluded domestic C corporations. Treasury's new interpretation reads into the statute a rule Congress rejected.
- **It reverses decades of well-settled law.** Treasury's interpretation of the statute is contradicted by the structure and legislative history of Section 897, the only IRS ruling on the topic and judicial opinions concerning the application of constructive ownership rules generally.
- **The look-through rule is retroactive and disruptive.** It imposes the regulations on investment structures in place for years and creates significant uncertainty for foreign investors in REITs and infrastructure.
- **It impedes investment in the U.S. economy.** Foreign capital as a share of total U.S. CRE investment has already fallen from over 16 percent in 2018 to less than 6 percent in 2024. The rule risks further reducing capital formation for job-creating U.S. real estate and infrastructure projects.
- **The legal case against the look-through rule is even stronger today** in the wake of the Supreme Court's *Loper Bright* decision, in which the Court significantly narrowed the deference to which regulatory agencies are entitled when rulemaking.
- **Treasury should formally withdraw the rule and issue sub-regulatory guidance** allowing taxpayers to rely on the forthcoming withdrawal. Restoring certainty in FIRPTA policy is essential to re-attracting global capital to U.S. real estate.

The federal government should reform FIRPTA and work to remove tax barriers that deter capital formation and investment in U.S. real estate and infrastructure.

- Foreign investment is a major source of capital for U.S. commercial real estate, leading to job creation and economic growth for communities throughout our nation.
- While RER supports efforts to protect national security as well as the integrity of commercial real estate investments, we have concerns about rules that may hinder foreign investment in U.S. real estate by legitimate enterprises and capital formation by law-abiding entities.
- Many investment funds that are controlled or advised by regulated U.S. asset managers source investment capital in global capital markets.
- With approximately $1.5 trillion of U.S. commercial real estate debt coming due in the next three years, foreign equity investments in U.S. assets are often an important source of capital as commercial real estate owners seek to restructure, refinance or sell their properties.
- Discouraging foreign investment weakens U.S. competitiveness, raises the cost of capital for U.S. developers and undermines efforts to revitalize urban cores, modernize infrastructure and expand the housing supply.

Additional Resources

- Roundtable Weekly, "Coalition Urges Treasury to Withdraw FIRPTA Look-Through Rule" (March 21, 2025)
- RER letter, "Re: Request for Expedited Withdrawal of Final Regulations on 'Domestically Controlled Qualified Investment Entities'" (March 20, 2025)
- RER letter, Background and Analysis (March 20, 2025)