



The Real Estate Roundtable

Business Interest Deductibility

Tax Policy

Summary

The 2017 tax bill included strict new limits on the deductibility of business interest, generally restricting this to 30 percent of the taxpayer's EBITDA (earnings before interest, tax, depreciation, and amortization). However, the bill also included a key provision that allows commercial real estate (a real property trade or business) to opt out of the interest limitation. The One Big Beautiful Bill Act (OB3 Act) included a provision that will allow more real estate businesses to fully deduct their business interest and qualify for 100 percent bonus depreciation on their nonresidential, interior improvements.

Key Takeaways

- 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.
 - The ability to finance investment and entrepreneurial activity with borrowed capital has driven jobs and growth in the U.S. for generations. America's capital markets are the deepest in the world and provide our economy with a valuable competitive advantage.
 - **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.
-

Background

Business Interest and Depreciation

- The final 2017 tax 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. It also included 100 percent expensing of leasehold and nonresidential interior improvements for five years, phasing down thereafter.
- The 30 percent interest limit did 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.
- The OB3 Act reinstated (effective Jan. 1, 2025) and permanently extended a broader EBITDA definition of income for purposes of the section 163(j) limit on business interest. This change will allow many taxpayers to own and operate commercial real estate under the general §163(j) business interest limitation, a requirement for 100 percent expensing of leasehold and interior improvements.
- Following passage of the OB3 Act, RER asked Treasury to issue guidance allowing taxpayers to retroactively modify or revoke prior elections out of the interest deductibility limits in order to benefit from the fully restored bonus depreciation incentive in the legislation ([RER letter, Oct. 17, 2025](#)). This relief was issued in March 2026 in the form of subregulatory tax guidance ([IRS Rev. Proc 2026-17](#)). The guidance will spur new property improvements while ensuring that existing property owners are able to avail themselves of an important benefit included in the OB3 legislation.

Recommendations

Avoid New Restrictions on Business Interest Deductibility: 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.

- New restrictions on interest deductibility would cause enormous damage to U.S. commercial real estate



Business Interest Deductibility

The Real Estate Roundtable

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.

- The change to the EBITDA/163(j) definition in the OB3 Act is a positive development that will allow more real estate businesses to fully deduct their interest while also expensing their property improvements and upgrades. The change will accelerate the modernization and repositioning of real estate assets that is critical to meet post-pandemic business needs.
- Congress should avoid changes to cost recovery rules, such as shorter depreciation schedules, if they are paid for or offset with reforms that deny real estate owners' ability to deduct borrowing costs, an ordinary and necessary business expense.