The Real Estate Roundtable
Pass-Through Taxation
Tax Policy

Summary

Real estate generally is owned and operated through "pass-through" entities that allow income to pass through to individual owners rather than taxing the income at the entity level. Pass-through entities such as partnerships, limited liability companies (LLCs), S corporations, 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.

Congress permanently extended the 20-percent pass-through deduction in the One Big Beautiful Bill Act (OB3 Act), signed into law on July 4, 2025. More recently, Democratic members of Congress have introduced legislation to repeal the pass-through deduction for taxpayers with incomes over $1 million and restructure partnership taxation.

Over the last two years, RER has submitted three amicus briefs (e.g., RER submission in *Soroban*, December 2025) in support of taxpayers challenging the government's recent assertion that limited partners are subject to self-employment taxes (SECA) unless the LP is also passive investor. The government position, which could have significant negative consequences for real estate partnerships, is inconsistent with the intent, language, and spirit of the 1977 statute that exempts limited partners from SECA.

Key Takeaways

- 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.
- 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.
- Publicly traded REITs allow small investors to invest in diversified, commercial real estate using the same single tax system available to partners and partnerships.
- Small and closely-held businesses drive job growth and entrepreneurial activity in the U.S. Entity choice is a differentiator that contributes to our entrepreneurial culture.

Background

Pass-Through Business Income Deduction

- Congress enacted a 20 percent deduction for pass-through business income in the Tax Cuts and Jobs Act of 2017 (Section 199A).
- The pass-through deduction applies to pass-through income to the extent the business pays wages to employees and/or owns tangible, depreciable property (such as real estate). Specified services businesses (e.g., law firms, accounting firms, etc.) are not eligible for the deduction.
- Section 199A lowers the top marginal income tax rate on qualifying pass-through business income from 39.6 percent to 29.6 percent.
- Section 199A was scheduled to expire at the end of 2025. The OB3 Act permanently extended the pass-through deduction.
- Legislation introduced after enactment of the OB3 Act by a handful of House Democratic members (*Equal Tax Act*, H.R. 5336) would repeal Section 199A for business owners with annual incomes over $1 million.
- Also in 2025, Senate Finance Ranking Democrat Ron Wyden (D-OR) proposed comprehensive reforms to restructure partnership taxation. The *PARTNERSHIPS Act* (S. 2095) would increase the tax burden on partnerships by an estimated $727 billion over the next 10 years.

Recommendations

Preserve Pass-Through Tax Rules and Section 199A: 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.

- 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, and it should be retained.
- Section 199A helps preserve tax fairness vis-à-vis large corporations, promoting competition and entity choice.
- In addition, Congress should avoid partnership tax reforms that will discourage capital formation, make it harder to contribute property to a partnership, or undermine the ability to finance partnership operations and activities. Congress should also avoid tax reforms that retroactively and unfairly change the economics of prior transactions.
- Lastly, fundamental changes such as rewriting or reinterpretation of the limited partner exception from self-employment taxes should be considered through the legislative process, not by administrative fiat.