Tax Policy

The Roundtable focuses on maintaining a competitive U.S. tax code that encourages capital formation, rewards entrepreneurial risk-taking, and supports jobs and communities.

Rational taxation of real estate assets and entities, grounded in the economics of underlying transactions, promotes job creation and responsible development. From the President's budget to infrastructure and energy legislation to the debt ceiling and deficit reduction, tax proposals are often central to the major economic policy debates in Washington.

Last year was no different as real estate-related tax increases were raised and considered in the context of the *Inflation Reduction Act (IRA) of 2022*, President Biden's signature economic legislation. In response, The Roundtable coordinated advocacy efforts across the industry, challenged specific proposals using fact-based research and analysis, and engaged lawmakers on a sustained basis with positive results. The final legislation dropped harmful tax provisions while simultaneously expanding tax incentives for productive investment in energy-saving building improvements.

The Roundtable's tax policy efforts in 2022 and 2023 helped ensure lawmakers understood and appreciated the importance of tax rules that promote capital investment, preserve flexibility in the choice of entity, and support economic development and affordable housing.

Initial versions of tax reconciliation legislation included higher tax rates on capital gains and rental income, greater tax burdens on partnerships and pass-through businesses, and more restrictive rules on carried interest.

Working with industry partners and other stakeholders, The Roundtable demonstrated effectively how increasing capital gains taxes and reducing incentives for entrepreneurial risk-taking would adversely affect workers and communities. The final *Inflation Reduction Act* dropped tax increases that were squarely aimed at capital gains, real estate, and entrepreneurship but still generated an estimated $750 billion in deficit reduction through a combination of spending and revenue measures, such as a new minimum tax on large corporations and an excise tax on stock buyback transactions.

There is more work to do to ensure that new and recently elected lawmakers understand and appreciate the interconnection between real estate taxation, jobs, and communities. In 2017, Congress passed the most significant reforms to the federal tax code since 1986. Over the next few years, many of the reforms will expire, triggering new congressional deliberations over real estate-related tax rules.

Today, 80% of the majority members of the tax-writing committee were not privy to the key debates that decisively resolved several tax issues fundamental to real estate investment, development, and ownership.

Chairman of the House Ways and Means Committee Rep. Jason Smith (R-MO) outlines the committee's recent tax proposals impacting commercial real estate.

Senate Republic Whip John Thune (R-SD) discusses monetary policy with Roundtable members.

Going forward, The Roundtable will continue educating lawmakers regarding the importance of long-standing tax rules related to capital gains, interest deductibility, like-kind exchanges, carried interest, partnerships and REITs, foreign investment, and much more. Our external research and analysis, the gathering and synthesis of credible data from industry leaders, and our continuous engagement with members of Congress and the administration will lay the foundation for another successful tax debate.

While our industry is preparing for another wide-ranging and consequential tax bill, we are working opportunistically to advance tax changes aimed at specific and immediate concerns, such as housing affordability, commercial-to-residential property conversions, Opportunity Zone tax incentive deadlines, REIT-related party rules, and others. We are also challenging misguided regulatory actions that threaten to reduce access to foreign capital for U.S. real estate and infrastructure investments.

Capital Gains/Unrealized Gains

The United States has traditionally taxed long-term capital gains at a lower rate than ordinary income (wages, rent, and other compensation). Today, long-term capital gains are taxed at a top rate of 20%, but the rate rises to 23.8% if the income is subject to the 3.8% tax on net investment income.

Maintaining a reduced tax 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. Congress must continue to encourage investment and job creation with a meaningful capital gains incentive.

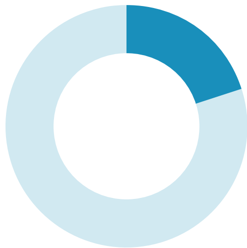
The administration has proposed nearly doubling the long-term capital gains rate and adding a new retroactive, annual minimum tax on the unrealized gains of wealthy taxpayers. Senior lawmakers, such as Senate Finance Chairman Ron Wyden, have introduced similar proposals to tax unrealized gains. By taxing business assets and investments annually, a “mark-to-market” tax on unrealized gains would remove one of the major incentives for patient, productive capital investment.

The Roundtable and other stakeholders were successful in persuading lawmakers to avoid raising taxes on capital investment (capital gains or unrealized gains) in the *IRA*, which passed in August 2022. However, The *IRA* did include a new corporate alternative minimum tax (CAMT), which levies a 15% minimum tax on the book income of certain large corporations. In March 2023, The Roundtable joined several other trade organizations in submitting comments to the IRS urging the administration to clarify that unrealized gains and losses should not be subject to tax under the new CAMT. This clarification would prevent patchwork rules that leave certain categories of unrealized gains and losses subject to tax.

Sen. Kyrsten Sinema (I-AZ) played a vital role ensuring carried interest provisions were not included in the Inflation Reduction Act (IRA) of 2022.

Like-Kind Exchanges

The ability to defer a capital gain through a like-kind exchange (LKE) is an essential element of the current tax system—dating back to 1921.



Close to 20% of all commercial real estate transactions involve an LKE.[10]

These exchanges are fundamental to the health and financing of our industry. They lower the cost of capital and spur investment, particularly during times of market volatility.

President Biden has repeatedly proposed restricting gains deferred through real estate like-kind exchanges to no more than $500,000 per year, or $1 million in the case of a married couple.

Ernst and Young and the Real Estate Like-Kind Exchange Coalition, which includes The Roundtable, partnered to produce a report detailing the importance of LKEs to the U.S. economy.

Economic Activity Supported By LKE Rules in 2021[11]

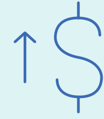
976,000 Jobs

$48.6B In Wages and Benefits

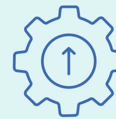
$97.4B Contributed to U.S. GDP

These and other studies have found that LKEs:

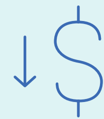
Increase net investment



Boost tax revenue

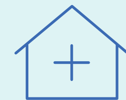


Stimulate capital expenditures leading to job growth



Reduce leverage and financial risk

Lower rents for households



Support healthy property values

The Roundtable will continue raising the awareness of policymakers and the public regarding the understated contribution of like-kind exchange rules to jobs and business growth, housing affordability, and the economic well-being of local communities.

Partnerships & Pass-Through Taxation

Real estate is generally 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. Half of the country's four million partnerships are real estate partnerships. Closely held partnerships and pass-through businesses allow owners and investors with diverse interests and expertise to pool their resources by flexibly allocating the risks and rewards of the venture. In so doing, partnerships contribute to America's dynamic, entrepreneurial culture.

Estimated Employment, Income, and Output Effects of Real Estate Industry Partnerships and LLCs in the U.S.[12]

9,044,356

Employment- Workers

$518.5B

Labor Income

$896.8B

Value Added

$1,272.2B

Output

Real estate partnerships have contributed to the employment of over **9 million workers, $518 billion of labor income, and $897 billion of value added to U.S. GDP.**

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.[13]

In 2017, Congress reduced the corporate tax rate by 40% and created a new 20% deduction (section 199A) for pass-through business income.

In the last Congress, an early version of tax reconciliation legislation would have raised the top marginal income tax rate on many small and pass-through business owners from 29.6% today to 46.4%. Specific tax increases in the House bill included capping the section 199A pass-through deduction, increasing the top ordinary income tax rates, expanding the net investment income tax, and creating a new surtax on incomes over $5 million. President Biden's current budget includes similar proposals. The Roundtable successfully made the case to lawmakers that these changes would create a historically high differential in the tax rates between pass-throughs and C corporations and put pass-through businesses at a competitive disadvantage. They were dropped from the final version of the *Inflation Reduction Act*.

The pass-through business income deduction is scheduled to expire at the end of 2025. The Roundtable is working with stakeholders to build the case for preserving an equitable playing field for partnerships and pass-through businesses by permanently extending section 199A.

Carried Interest

Carried interest is the interest in partnership profits a general partner receives for managing an investment and bearing the entrepreneurial risk of a venture. It is a vital tool that contributes to real estate capital formation and new housing development, productive risk-taking, and job creation.

In the last Congress, several members reintroduced legislation to recharacterize all carried interest income as ordinary income. Legislation passed by the House Ways and Means Committee would have extended the holding period required for carried interest to qualify as capital gains and would have made other substantive changes to carried interest rules unfavorable to general partners.

A 2021 study by USC Professor Charles Swenson drew on Roundtable-provided data and estimated the economic damage caused by increasing taxes on carried interest.

Long-Run Economic Impact of Carried Interest Legislation[14]

1.77M	Real Estate-Related Job Losses
$11.22B	Reduction in Federal Tax Revenue
$26.74B	Reduction in State/ Local Tax Revenue

A Roundtable-led letter to Congress from 15 national real estate trade organizations last August warned lawmakers that new restrictions on carried interest would slow housing production, discourage the capital needed to re-imagine buildings to meet post-pandemic business needs, hamper job creation and create added uncertainty in an already confusing economic environment. The carried interest changes were dropped from the reconciliation bill before it passed the full House. An effort to add back the carried interest provisions in the Senate was rebuffed by key moderates such as Senator Kyrsten Sinema.

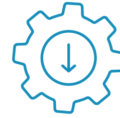
Step-Up In Basis

The United States levies a comprehensive estate tax at rates as high as 40% on a decedent's wealth and assets, including unrealized gains. 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.

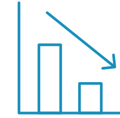
President Biden's budget would end the step-up in basis of assets and impose income tax on a decedent's unrealized gains at the time of death. By extending the income tax to a decedent's appreciated assets, the administration would double tax individuals when they die–first through an income tax on appreciated assets and second through the comprehensive estate tax. Such efforts would be punitive and confiscatory and force many family-owned and closely-held real estate businesses to liquidate.

Last Congress, The Roundtable and other members of the Family Business Estate Tax Coalition commissioned Ernst and Young 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 the same period.

Impact of Repealing Step-Up in Basis[15]



40,000 jobs would be lost every year in the first 10 years since enactment



GDP would decrease by **$50 billion over 10 years**

The Roundtable is collaborating with a wide range of stakeholders to advocate for and support the fair and reasonable taxation of inherited wealth.

FIRPTA

The *Foreign Investment in Real Property Tax Act (FIRPTA)* imposes a discriminatory capital gains tax on foreign investments in U.S. real estate that does not apply to any other asset class. The *FIRPTA* regime discourages capital formation and investment that could be used to create jobs and improve U.S. real estate and infrastructure.

FIRPTA does not apply to foreign investment in a domestically controlled REIT. In December 2022, Treasury and the IRS released proposed regulations to redefine what constitutes a domestically controlled REIT and impose capital gains taxes, through *FIRPTA*, on legal structures that taxpayers have used for decades when planning real estate and infrastructure investments. REITs, previously exempt from *FIRPTA*, would be thrust, retroactively, into the discriminatory tax regime. Further, the rule could impair real estate's access to foreign capital at a critical economic juncture and undermine foreign investors' confidence in the stability and predictability of U.S. tax rules. The Roundtable submitted comments to Treasury urging the withdrawal of the proposed look-through rule. The Roundtable and others also wrote to the congressional tax-writing committees asking members of Congress to encourage Treasury and the IRS to withdraw the rule.

In addition, The Roundtable has supported bipartisan legislation in the House of Representatives to extend an important *FIRPTA* exception for foreign owners of publicly traded U.S. REITs to non listed REITs as well.

Opportunity Zones[16, 17]

Opportunity Zone (OZ) investments qualify for reduced capital gains taxes. By promoting long-term investment, economic development, and job growth in low-income areas, OZs are having a positive impact on local communities:

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 OZs by 11%.

Housing is Leading the Way: Through March 2023, Opportunity Funds focused on building much-needed housing-either entirely or as a component of their business strategy-have raised over

$28 billion

in equity from investors, outraising other categories such as commercial, hospitality, and renewables.

The Roundtable is encouraging Congress to pass the bipartisan, bicameral *Opportunity Zones Transparency*, *Extension*, and *Improvement Act*, which would extend expired OZ deadlines and allow OZs to continue spurring investment and economic development. The legislation would also improve OZ reporting and transparency, helping ensure that OZs serve the needs of local communities and fulfill their original promise.

In addition, The Roundtable is working to advance other modest but meaningful tax changes that would create or preserve jobs, aid local communities, and boost investment and economic growth.

These measures include the bipartisan *Retail Revitalization Act*, which would help landlords keep retail businesses alive, and save jobs in the process, by liberalizing the REIT-related-party rules that taint rental income received by a REIT from a tenant with whom it has an equity or debt interest. They also include the bipartisan *Fair Accounting for Condominium Construction Act*, which would modernize the outdated percentage-of-completion tax accounting rules that discriminate against condominium construction. The bill would reduce the cost of building new housing, especially in high-cost areas where density is needed.

(R-L): Senator Bob Menendez (D-NJ) discusses FIRPTA legislation with RER President & CEO Jeffrey DeBoer.