



The Real Estate Roundtable

**Washington & Legislative Update**  
**NAREC 2023 Annual Financial and Tax**  
**Conference**

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The Real Estate Roundtable  
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[www.rer.org](http://www.rer.org)

# The Real Estate Roundtable

- Brings together leaders of the nation's top publicly-held and privately-owned real estate ownership, development, lending and management firms with the leaders of major [national real estate trade associations](#) to jointly address key national policy issues relating to real estate and the overall economy.
- Seeks to ensure a cohesive industry voice is heard by government officials and the public about real estate and its important role in the global economy.
- Roundtable members' portfolios contain over 12 billion square feet of office, retail and industrial properties valued at more than \$4 trillion; over 4 million apartment units; and in excess of 5 million hotel rooms.

## Real Estate Trade Organizations

**10%**

American Hotel & Lodging Association (AHLA)	NAIOP, the Commercial Real Estate Development Association (NAIOP)
American Resort Development Association (ARDA)	National Apartment Association (NAA)
Association of Foreign Investors in Real Estate (AFIRE)	National Association of Home Builders (NAHB)
Building Owners and Managers Association Int'l. (BOMA)	National Association of Real Estate Investment Managers (NAREIM)
CCIM Institute (CCIM)	Nareit (NAREIT)
CRE Finance Council (CREFC)	National Association of Realtors® (NAR)
CREW Network (CREW)	National Multifamily Housing Council (NMHC)
International Council of Shopping Centers (ICSC)	Pension Real Estate Association (PREA)
Mortgage Bankers Association (MBA)	Real Estate Executive Council (REEC)
	Urban Land Institute (ULI)



## Asset Managers

**3%**

## Financial Services

**20%**

58% Banks (Commercial & Investment)
26% Insurers
16% Mortgage Bankers

## Owners

**67%**

55% Private	12% Hotel
44% Public	11% Housing
46% Mixed	4% Industrial
14% Office	2% Other
12% Retail	

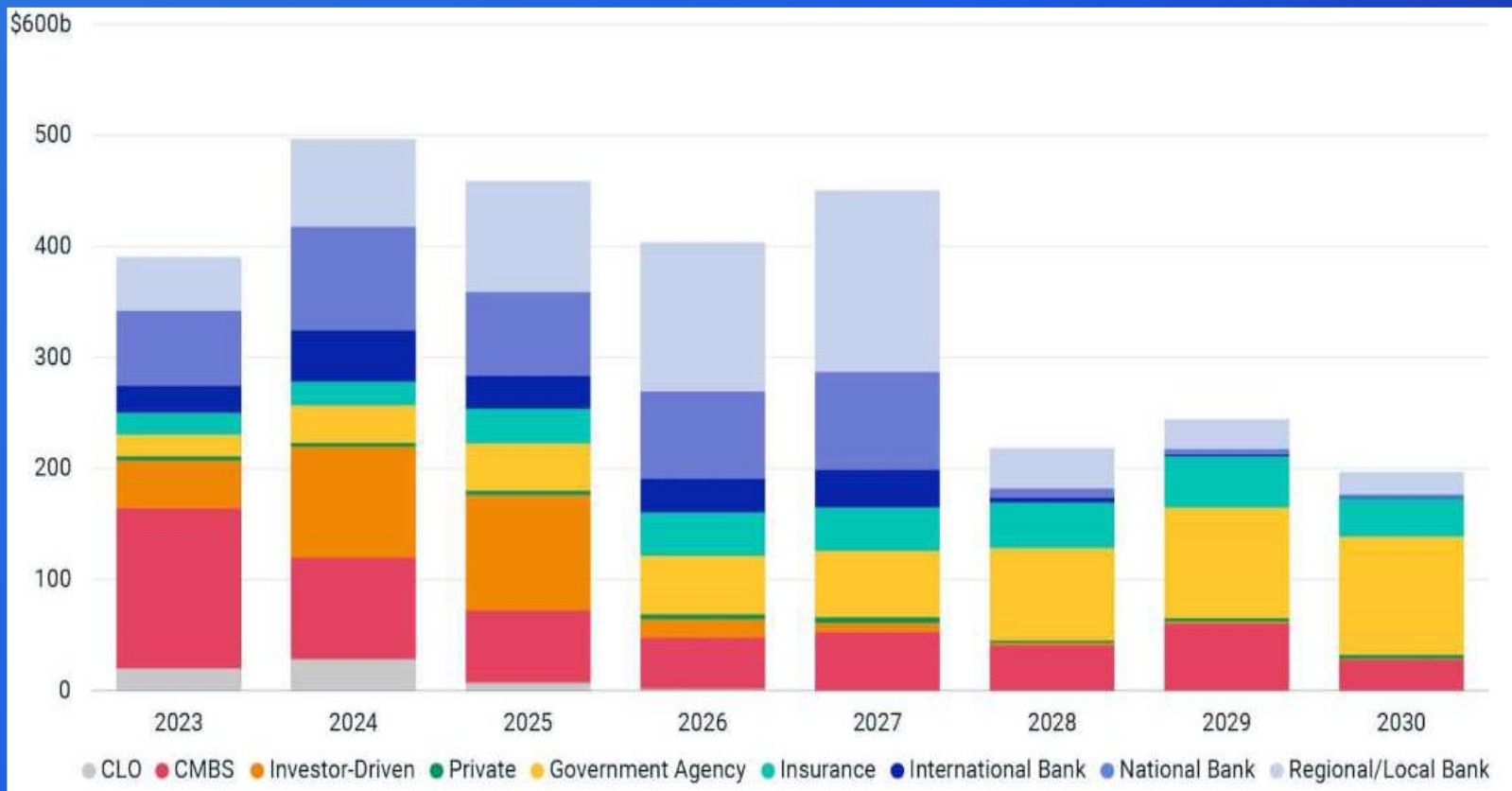
# Commercial Real Estate: Macroeconomic Environment

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- \$5.5 trillion of CRE debt outstanding with \$1.5 trillion maturing over next 3 years
  - Almost all outstanding CRE debt issued in a near-zero interest rate environment (2009-2022)
  - Loans were conservatively underwritten with strong debt service coverage and low loan-to-value ratios

# Commercial Real Estate: Macroeconomic Environment

## Volume of Maturing Commercial Real Estate Loans



Source: CBRE Research (June 2023)

# Commercial Real Estate: Macroeconomic Environment

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- Historically rapid rise in interest rates
  - 10 hikes over 14-month period
- Tighter credit conditions
  - Reduced lending by institutions, irrespective of the interest rate
- Elevated uncertainty regarding future leasing revenue
  - Back to the office?
- Limited price discovery
  - Few transactions occurring
- Steep decline in values for certain asset classes

# Commercial Real Estate: Responding to Macroeconomic Challenges

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Consequence: Markets need time to stabilize, find price discovery. Borrowers need time to restructure their debt (CRE loans require additional equity)

## RER Policy Recommendations (3/17/23 letter)

Banking regulators should reestablish troubled debt restructuring guidance similar to 2009, 2010, 2020, and 2022 that increases flexibility and encourages financial institutions to work with borrowers to develop responsible, constructive refinancing plans

Treasury should withdraw proposed regulations imposing new tax barriers on foreign investment in U.S. real estate that further reduce access to capital and equity at a time when it is most needed (e.g., proposed FIRPTA regulations redefining a domestically controlled REIT)

Regulators should avoid pro-cyclical increases in capital requirements for U.S. banks that limit their ability to provide credit to businesses in need

# President Biden's Tax Agenda and Commercial Real Estate

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## Capital Gains Rate

- Increase the top, combined tax rate on long-term capital gains from 23.8% to 44.6%.
  - Capital gains rate increased from 20% to 39.6%
  - Net investment income tax increased from 3.8% to 5%.

## Mark-to-Market Tax on Unrealized Capital Gains

- Establish a retroactive, annual minimum tax of 25% on the income and unrealized gains of taxpayers with wealth (assets minus liabilities) exceeding \$100M.

# President Biden's Tax Agenda and Commercial Real Estate

## Real Estate Professionals

- Extend the 3.8% net investment income tax to real estate professionals and other pass-through business owners who are currently exempt from the tax because they are active in their business.

## Like-kind exchanges

- Cap the annual deferral of gain from real property like-kind exchanges to \$500K for an individual, \$1M for a married couple

## Carried interest

- Tax all carried interest income (profits interests) at ordinary income rates

# President Biden's Tax Agenda and Commercial Real Estate

## Taxation of gains at death

- Repeal stepped-up basis of assets at death and replace with regime that taxes unrealized gains at time of transfer by gift or death
  - \$1M exclusion + \$250K for principal residence
  - Carryover basis for family-owned and operated businesses

## Active pass-through business income (461(l))

- TCJA limits deductibility of active losses in excess of \$250K/\$500K against wage and investment income. Active losses are deferred for one year, before their inclusion in a taxpayer's NOL.
- President would permanently compartmentalize active losses, disallow use against wage/investment income

# President Biden's Tax Agenda and Commercial Real Estate

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## Depreciation

- Recapture and tax real estate depreciation deductions at ordinary income tax rates

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# President Biden's Tax Agenda and Commercial Real Estate

## Affordable housing / urban development

- Increase the supply and availability of affordable housing by enhancing and expanding the low-income housing tax credit (\$28 B)
- Establish a new neighborhood homes tax credit for the development of affordable, owner-occupied housing (\$15 B)
- Incentivize State, local, and regional jurisdictions to remove barriers to affordable housing developments, such as restrictive zoning (\$10 B)
- Permanently extend new markets tax credit (\$7 B)

# Inflation Reduction Act

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- One-year anniversary on Aug. 16, 2023
- \$790 billion legislation
  - 15% minimum tax on large corps (book income > \$1B)
  - 1% excise tax on stock buybacks
  - \$370 B in climate investment
    - \$100B federal spending
    - \$270 B tax incentives
- Regulatory implementation ongoing

# Inflation Reduction Act and Real Estate

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## 1% Stock buyback excise tax

- REITs exempt

## 15% Corporate alternative minimum tax (CAMT)

- REITs exempt
- Income aggregated if separate entities are treated as a single employer under §52(a) or (b), *but* §212 activities for the production or collection of income do not constitute a trade or business activity that requires aggregation

# Inflation Reduction Act and Real Estate

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## Energy efficient commercial buildings deduction (§179D)

- Special deduction for investments that generate whole building energy efficiency gains
- Enacted in 2005, minimal take-up outside public-sector buildings
- Post-IRA:
  1. lowers energy improvement requirement;
  2. creates sliding scale (larger deduction for greater energy savings);
  3. increases benefit 5x if project complies with prevailing wage/apprenticeship rules; and
  4. establishes alternative retrofit regime for buildings 5 years or older; REIT fix

# Inflation Reduction Act and Real Estate

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## Energy investment tax credit (§48)

- Pre-IRA: the credit for new solar energy and other property was phasing down from 30% today to 10% in 2026 and thereafter.
- Post-IRA:
  1. Creates two-tier credit 6%/30% based on compliance with prevailing wage and apprenticeship rules
  2. Bonuses for low-income census tract, domestic content, low-income housing or benefit
  3. Extends credit to energy storage technology, dynamic glass, microgrid controllers, linear generators
  4. Projects built after 2024 are subject to new, “zero carbon,” technology-neutral version of the credit (§48E)
  5. Phases out after 2032 or when national emissions target hit
  6. Credit transferable to unrelated parties (key for REITs)

# Inflation Reduction Act and Real Estate

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## EV charging stations (§30C)

- Pre-IRA: the 30% tax credit for alternative fuel refueling property (max \$30K per location) expired at the end of 2021.
- Post-IRA:
  1. Reinstates the credit through 2032
  2. Sets two-tier credit rate (6% / 30%) based on compliance with labor rules
  3. Credit limit increased to \$100K for each charging station installed at a property
  4. Eligibility limited to property located in a low-income census tract or non-urban area
  5. Credit transferable to unrelated parties (key for REITs)

# Inflation Reduction Act and Real Estate

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## **New energy efficient homes credit (\$45L)**

- Pre-IRA: \$1K/\$2K tax credit for developers of new energy efficient homes expired at the end of 2021.
- Post-IRA:
  1. Reinstates the credit through 2032
  2. Creates 4-tiered credit rate per dwelling unit (\$500/\$1,000/\$2,500/\$5,000) based on compliance with labor rules and extent of energy savings
  3. Highest multifamily standard (DOE's Zero Energy Ready Home Multifamily Program) still in development
  4. Labor rules: apprenticeship requirement not apply to multifamily construction; prevailing wage requirement not apply to single-family construction

# Inflation Reduction Act and Real Estate

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## Prevailing Wage / Apprenticeship Rules

- Pre-IRA, prevailing wage and other Davis-Bacon requirements generally applied to federally contracted projects but did not apply to private, commercial activities.
- Post-IRA:
  - Project must comply with certain labor-related rules qualify for bonus tax benefit that is 5x larger than the base benefit.
  - Two requirements:
    1. Pay DOL prevailing wages for the locality
    2. Individuals participating in registered apprenticeship programs must provide 10-15% of the labor hours

# Tax Legislative Outlook: *Who Wants What?*

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## **Congressional Democrats / Administration:**

- Child tax credit expansion / refundability
- Housing tax incentives
- Upper-income / corporate tax revenue

## **Congressional Republicans:**

- TCJA business tax extenders
- TCJA permanency
- Small business / farm tax relief
- Rollback of IRA green tax incentives and the IRS funding increase

# Tax Legislative Outlook: Affordable Housing

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15 years of underproduction has resulted in severe shortage of housing supply and a crisis of housing affordability.

## **Bipartisan Affordable Housing Credit Improvement Act (S. 1557, H.R. 3238)**

- Restores 12.5% allocation increase (exp. 2021)
- Increases credit allocations 50% over 2 years
- Decreases PAB-financing requirement from 50% to 25% for 4 percent LIHTC projects
- Basis boosts for rural, extremely low-income, and bond-financed developments
- Creates flexible income test for existing tenants
- Estimated to generate 1.9 million additional affordable rental homes over 10 years

# Tax Legislative Outlook: Property Conversions

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Post-pandemic conversion of underutilized or vacant buildings to better uses offers economic, social, and environmental benefits

RER proposal based on **Revitalizing Downtowns Act** in 117<sup>th</sup> Cong.

- Transferable tax credit to convert older, underutilized commercial real estate to housing (modeled on historic rehabilitation tax credit)
- 20% credit for qualifying conversion expenditures; 30% credit for properties in low-income census tracts
- Affordable housing requirement—three options
  - 20% of residential units reserved for individuals 80% of AMI
  - Owner enters into binding agreement with state or locality on affordable housing component
  - Building meets requirements of state or local law incentivizing conversion of commercial properties o

# Tax Legislative Outlook: Business Interest

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Tax Cuts and Jobs Act of 2017 (TCJA) limited deductibility of business interest to 30% of modified adjusted gross income (MAGI).

- Broader definition of MAGI expired at end of 2021
- **Real estate exception:** real estate can elect out of business interest limit, but then subject to longer cost recovery
- House W&M-passed **Build It in America Act** would extend taxpayer-favorable MAGI definition through 2025

# Tax Legislative Outlook: Bonus Depreciation

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**Pass-through income.** TCJA created 20% deduction for qualified pass-through business income.

- Permanently extend §199A (House Republicans)
- Limit maximum deduction under §199A to \$400K for an individual and \$500K for a married couple (House W&M Democrats)
- Phase out §199A for taxable incomes over \$400K (Chairman Wyden)

**Bonus depreciation.** Immediate expensing of capital investment phasing down after 2022

- House W&M-passed **Build It in America Act** would extend 100% bonus depreciation through 2025

# Tax Legislative Outlook: Debt Workouts

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Changes to a debt instrument's yield, collateral, payment schedule, and more can be treated as a taxable sale or exchange of the note

- Cancellation of debt income (CODI)—can arise whether or not borrower retains the real estate
- CODI exceptions include bankruptcy, insolvency, and real property business indebtedness
- Real property business indebtedness
  - Borrower cannot be a C corp.
  - Property cannot be dealer property
  - Debt must be incurred to acquire/construct/improve
- RER past proposal: CODI exclusion up to \$250K without tax attribute reduction, CODI exclusion for amounts above \$250K if tax attributes reduced

# Tax Legislative Outlook: Opportunity Zones

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Enacted in 2017 to spur economic growth and development in low-income communities. Temporary capital gains incentives are phasing down, some have already expired.

- **Bipartisan Opportunity Zones Transparency, Extension, and Improvement Act:**
  - Extends the initial capital gains deferral period for prior gain that is rolled into an QOF beyond 12/31/26
  - Shortens the 5/7-year holding period required for basis-step-up of prior gain
  - Sunset certain high-income census tracts
- House W&M-passed **Small Business Jobs Act** creates special rules for rural OZs, established information reporting and transparency rules for all Opportunity Funds

# Tax Legislative Outlook: REITs

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## Retail Revitalization Act / REIT constructive ownership rules

- Raises ownership threshold so that REITs can inject capital in struggling retail tenants without violating REIT related party rules (House-introduced)
- Modifies constructive ownership attribution test to reduce unintended and inappropriate attribution of ownership for purposes of REIT related party rules (House W&M)

## Parity for Non-Traded REITs Act

- Extends to non-traded REITs the safe harbor that allows a foreign shareholder to own up to 10% of a publicly traded REIT without triggering FIRPTA liability

# Tax Legislative Outlook: Condo construction

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## **Fair Accounting for Condominium Construction Act**

- Extends the completed contract method of accounting to new condominium construction, thereby aligning tax liability with actual cash income

# Tax Legislative Outlook: SALT

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- \$10K limitation on individual state and local tax (SALT) deduction expires at end of 2025
- Senate amendment to extended the SALT limit through 2026 removed from the Inflation Reduction Act
- House Democrats: increase cap on SALT deduction from \$10K to \$80K from 2021-2030; SALT cap dropped back to \$10K in 2031

# Tax Legislative Outlook: Homeownership

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## **Bipartisan Neighborhood Homes Investment Act (S. 639, H.R. 3940)**

- Tax credit competitively allocated by state agencies
- Credit covers the gap between construction/rehab costs in distressed areas and home prices (limited to 35% of total development costs)
- Credit claimed after home is completed and occupied by eligible, income-tested homeowner

## **Bipartisan More Homes on the Market Act (H.R. 1321)**

- Increases principal residence capital gains exclusion from \$250K/\$500K to \$500K/\$1 million

# Tax Legislative Outlook: Carried interest

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**House Democrats:** Extend carried interest §1061 holding period from 3 to 5 years

- Create exception for gain related to a real property trade or business
  - But §1231 gain pulled into §1061 regime
- Start of holding period delayed until substantially all assets are acquired by the partnership
- Gain recognized when carried interest transferred in common nonrecognition transactions, even if no cash or liquidity generated (gift, death, transfer to family partnership, nontaxable reorganizations, etc.)

# Tax Legislative Outlook

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## Potential “vehicles” for tax legislation

1. ~~Debt ceiling increase~~
2. Farm bill reauthorization
3. Federal aviation system reauthorization
4. End-of-year omnibus spending bill

# Tax Legislative Outlook: *the Crystal Ball*

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## End-of-year bipartisan agreement that includes:

1. Child tax credit expansion
2. R&D expensing
3. Business interest deductibility—broader MAGI definition
4. Bonus depreciation
5. Rollback of 1099K rules
6. LIHTC expansion
7. Retirement provisions
8. Property conversion tax incentive

# Real Estate Roundtable: Tax Policy Principles

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1. The tax system should encourage capital formation (from domestic and foreign sources) and appropriate risk taking, while also providing stable, predictable, and permanent rules conducive to long-term investment.
2. Tax policy should ensure that the rules closely reflect the economics of underlying transactions—avoiding both excessive marketplace incentives and disincentives that can distort the flow of capital investment.
3. Tax policy should recognize that, in limited and narrow situations (e.g., affordable housing and investment in distressed, low-income communities), tax incentives are needed to address market failures and encourage capital to flow toward socially desirable projects.
4. Tax changes should provide well-designed transition rules that minimize dislocation in real estate markets.

# Key Tax Proposals: Roundtable Perspective

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## Capital Gains

- Rate: Reduced capital gains rate decreases the cost of capital, drives long-term investment, encourages productive entrepreneurial activity, attracts investment from around the world, and increases U.S. workforce productivity and competitiveness
- Like-kind exchanges: 10-20% of CRE transactions involve a LKE; exchanges are akin to tax-free corporate reorganizations and simply allow gains to stay fully invested in the underlying business; economically, LKEs are fundamental to the health and financing of CRE; they are facilitating critical repurposing of real estate assets post-COVID and supporting jobs, investment, and tax revenue.

# Key Tax Proposals: Roundtable Perspective

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## Capital Gains, cont'd

- Death: Unrealized, appreciated gains are taxed when an individual dies through the estate tax; policymakers should avoid the unfair and unintended economic consequences that would result from imposing a second tax on unrealized gains at death
- Carried interest: General partners assume significant risks unrelated to invested cash, including personal loan guarantees, construction financing, predevelopment expenses, litigation risk, and more; policymakers should not stifle entrepreneurial risk taking and sweat equity by recharacterizing gain derived from the appreciation of a capital asset

# Key Tax Proposals: Roundtable Perspective

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- Pass-throughs: Closely held partnerships and pass-through businesses drive job growth and entrepreneurial activity; tax increases should not disproportionately impact or discriminate against these entities vis-à-vis large, public corporations
- Unrealized appreciation: 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. The tax would remove an incentive for productive, long-term investment and is likely unconstitutional.



## The Real Estate Roundtable

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