Protecting Commercial Real Estate-Related Tax Provisions

Congressional Action Needed:

Though comprehensive tax reform is not likely to be enacted in 2015, key Members of Congress are still exploring the possibility of agreement on business-only tax reform with the Obama Administration. Lawmakers and their staffs must be educated about the vital role that commercial real estate tax provisions play in the nation's economy. Congress should oppose proposals that would repeal like-kind exchanges or extend depreciable lives of real estate.

Congressional Actions To Date:

- No viable comprehensive tax reform legislation has been introduced, but leaders of the tax committees (House Ways and Means and Senate Finance) have begun laying the groundwork for reform.

What To Tell Your Representatives And Senators:

- **Like-Kind Exchanges:** Since 1921, the Section 1031 provision has allowed investment real estate to be exchanged for property of a like-kind on a tax-deferred basis. Exchanges are essential in investment and commercial real estate transactions; if repealed, fewer redevelopment projects will go forward, resulting in fewer new jobs. The like-kind exchange provision provides liquidity to an illiquid asset. Repealing it would harm economic growth.
- **Leasehold Improvements:** A temporary provision permitting the cost of leasehold improvements to be recovered over 15 years has been in place for many years. Unfortunately, this provision expired at the end of 2014. Unless Congress extends the provision on a retroactive basis, all the costs of leasehold improvements placed in service on or after January 1, 2015, will need to be recovered over a 39-year period. This will make such investments less attractive and harm economic growth.

Issue Background:

While enactment of tax reform has little chance this year, the ideas promoted by House and Senate tax leaders will be on the table when Congress gets serious about moving tax reform. Members of Congress need to understand now that tax proposals that harm real estate are nonstarters.

Like-Kind Exchanges Must Be Retained

- Repealing the like-kind exchange provision would be counterproductive and result in the loss of jobs and economic growth with little gain in revenue.
- Two separate tax reform plans last year (Baucus and Camp) included repeal of Section 1031, and the President's budget this year again proposed a major cutback. Tax reform plans that include repeal of like-kind exchanges weaken the provision by making it more likely Congress will go along when tax reform becomes more serious.

Make Permanent the 15-year Depreciation Period for Leasehold Improvements

- Providing a shorter and more realistic depreciation period for tenant improvements allows for necessary upgrades in technology and property modernization.
- A shorter and more realistic depreciation period assures that nonresidential buildings will be adequately maintained and modernized.
- Shorter depreciation periods better reflect the natural wear and tear on improvements, along with technological obsolescence that can occur more quickly than physical wear and tear.
- Updated and well-maintained properties are more readily bought and sold.

Opposing Viewpoints:

- The like-kind exchange provision is a loophole that needlessly benefits those fortunate enough to own investment property. However, NAR and other real estate advocates point out that repeal or cutback of the provision would harm economic growth and job creation.
- The 15-year depreciation period needs an offset to make up the loss of dollars to the Treasury. However, most believe keeping long-standing tax policies in place should not have to be offset.

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