Tax Reform and Real Estate - 2015

2015 could be a year for major tax legislative activity as many in Congress have expressed support for tax reform that simplifies the system, increases economic growth and job creation, and reduces unfairness. The National Association of REALTORS® (NAR) is a major stakeholder in tax reform. A sizable majority of American families are homeowners (about 65%), and several provisions in the current tax law support this major tenet of the American Dream. In addition, many Americans hold real estate for investment purposes, and real estate is a principal asset for most business enterprises. Those holdings range from ownership of a single rental condo all the way to investments in huge agricultural land tracts and commercial buildings.

As the leading voice for real estate, NAR is providing you with information about our positions on a variety of real estate tax provisions. NAR supports retention of current-law tax provisions that encourage homeownership and real estate investment. Some current-law tax provisions related to investment in real estate are burdensome and should be modified. The following are our major real estate tax policy issues and concerns.

Mortgage Interest Deduction: NAR support current law, which permits homeowners to deduct the interest on up to $1 million of indebtedness on a principal residence and a second home. *NAR opposes any effort to reduce this limit or to impose rules that would reduce the tax and economic benefits mortgage interest deductions provide.*

State and Local Tax Deductions: The deduction for state and local taxes is the most frequently used deduction among taxpayers who itemize. Deductions are permitted for state and local income taxes and property taxes (both real property and personal property). This provision prevents double taxation on the same income. *NAR supports current law and would oppose legislation to curtail or eliminate this deduction, especially as it relates to real property tax.*

$250,000/$500,000 Exclusion on the Sale of a Principal Residence: This is among the most taxpayer-friendly provisions in the entire Internal Revenue Code. When an individual sells a principal residence, any gain on the sale is generally treated as a capital gain. In 1997, Congress excluded a large portion of gains on a principal residence from taxation. Up to $250,000 of gain may be excluded on tax returns filed as individuals, and up to $500,000 of gain may be excluded on joint returns. These dollar amounts are *not* indexed for inflation. This provision is important as a retirement planning tool for many older homeowners, and is also particularly useful for growing families. The provision also greatly simplifies tax compliance for millions of Americans. *NAR supports current law and would oppose any legislation that reduced or eliminated the $250,000/$500,000 amounts.*

Capital Gains: Under current law, most long-term capital gains are taxed at 15%. This reduced rate provides an incentive to make and hold productive investments. When an asset is sold, the low rate is a simplified proxy for indexing for inflation when property has increased in value. As real estate investments are generally held for many years, this reduced rate is fully justified. *NAR believes that sound tax policy requires a meaningful differential between the capital gains rate and the rates associated with taxation of ordinary income.*

Like-Kind Exchanges: Since 1921, the tax law has recognized that the exchange of one property held for investment or business use for another property of like kind results in no change in the economic position of the taxpayer and, therefore, should not result in the immediate imposition of tax. The like-kind exchange provision provides for a deferral of tax, not an exemption, and is key to the growth and health of our economy and to the real estate sector. *NAR supports the ability of investors to utilize tax-deferred like-kind exchanges and would oppose any legislation that would repeal or limit them for real estate.*

<u>Depreciation of Commercial and Investment Real Estate:</u> The current tax law requires commercial and investment real estate to be depreciated over a 39-year period, or over a 27.5 year period in the case of residential rental property. Because most real estate suffers significant obsolescence long before the buildings physically wear out, these recovery periods are too long. However, Congress should not exacerbate the problem by enacting even longer recovery periods as an offset to lower tax rates in a tax reform bill. *NAR would oppose legislation that lengthens the current depreciation periods of real property.*

<u>15-Year Cost Recovery For Qualified Leasehold Improvements:</u> Improvements made by or for tenants of commercial real property have an economic life far less than the 39 years over which the costs of nonresidential commercial real estate must be recovered under current law. This is why Congress enacted the provision allowing the costs of such improvements to be recovered over 15 years. Unfortunately, this provision was not made permanent in the tax law, and despite wide and deep support from both sides of the political aisle, the 15-year cost recovery period has again expired, making capital investment decisions harder for many businesses. *NAR supports a permanent extension of the 15-year recovery period for leasehold improvements.*