NMHC/NAA Viewpoint

As part of the Tax Cuts and Jobs Act of 2017, Congress extended multifamily depreciation periods to 30 years for real estate firms wishing to retain the full deductibility of business interest. Congress should consider proposals to shorten recovery periods while opposing measures to increase the 25 percent depreciation recapture rate applicable to sales.

TAX DEPRECIATION RULES

Tax depreciation rules enable multifamily developers to recover their investment, which promotes apartment construction, economic growth and job creation. Tax reform should ensure that depreciation tax rules match the economic life of assets by taking into account natural wear and tear, as well as technological obsolescence.

Today’s depreciation rules affect owners of multifamily properties in two ways. First, a property owner may take an annual tax deduction so that a multifamily property is fully depreciated over a 30-year period for firms electing to fully deduct business interest and a 27.5-year period for firms which elect to abide by limits on interest deductibility or are exempted by having average annual gross receipts under $25 million. Second, once a property is sold, the gain in a building’s value that is attributable to prior depreciation deductions is generally subject to a 25 percent tax known as depreciation recapture.

NMHC/NAA opposed extending depreciation periods or depreciation recapture tax rates during the 2017 tax reform debate and, instead, called on policymakers to consider shorter periods and lower rates. Recent research conducted by the MIT Center for Real Estate and PricewaterhouseCoopers has concluded that the depreciation of multifamily buildings should be approximately 19 years to truly reflect economic realities.

Raising taxes on depreciation recapture is also problematic and possibly counterproductive. After decades of operations, many multifamily owners have a very low tax basis in their properties. If they were to sell them, even under current law they would have to pay large depreciation recapture taxes. To avoid this tax bill, many current owners will not only avoid selling their properties, but they will also be reluctant to make additional capital investments in properties with little value. The result is deteriorating properties that are lost as safe, affordable housing. Increasing depreciation recapture taxes would only make the problem worse.

Depreciation rules that do not reflect the economic lives of multifamily buildings would result in less development and investment, reduce real estate values, and stifle industry’s ability to create new jobs.