



The National Multifamily Housing Council (NMHC) and the National Apartment Association (NAA) respectfully submit this statement for the record for the House Ways and Means Subcommittee on Oversight's July 14, 2021, hearing titled *Expanding Housing Access to All Americans*.¹

COVID-19 and Multifamily Housing

The apartment industry today plays a critical role in housing this nation's households by providing apartment homes to 40.1 million residents, contributing \$3.4 trillion annually to the economy while supporting 17.5 million jobs.² At the same time, it is apparent that the supply of multifamily housing is insufficient to meet the nation's housing needs. Moreover, the COVID-19 pandemic has laid bare the fragility of our housing infrastructure. Home should be a respite, and yet 2020 and 2021 have found many households challenged by a virus that unspooled the economy and their personal finances.

While Congress acted to make much-needed resources available to renters, the funds were, for a variety of reasons, slow to reach households in need. Unfortunately, many qualified applicants have yet to receive emergency rental assistance. Unmet rental payments have caused extreme hardship for many property owners who have not had the resources to continue to meet their financial obligations through the prolonged health crisis. As leaders of the apartment industry, NMHC and NAA members have worked with their residents to apply for rental assistance, modified rental agreements, and otherwise supported the members of their apartment communities throughout the pandemic.

NMHC and NAA pledge to work with our members who represent the leading owners, developers, and financiers of apartment properties to not only stabilize the multifamily sector, but also to leverage pandemic recovery efforts to improve the state of housing nationwide. This means delivering more units of housing that are broadly affordable in communities that have good jobs and schools and will support an economy of opportunity for hardworking Americans.

Looking Beyond COVID and Addressing the Housing Affordability Challenge

As the House Ways and Means Committee and Congress look beyond COVID-19 recovery and to expanding housing access to all Americans, it is critical to recognize that even prior to the pandemic, the country was facing a nationwide housing affordability challenge and a historic unmet demand for rental housing. Beginning in the mid-2000s, the nation experienced the greatest renter wave in its history, as the number of households who rent rose by more than 7 million.³ Fueled by this extraordinary demand for apartment homes, recent NMHC and NAA research finds that we need to build an average of 328,000 new apartments every year.⁴ Yet our industry faced significant challenges to new apartment construction, development and renovation before this crisis, and we have only hit that mark four times since 1989.⁵

¹ For more than 20 years, the National Multifamily Housing Council (NMHC) and the National Apartment Association (NAA) have partnered in a joint legislative program to provide a single voice for America's apartment industry. Our combined memberships are engaged in all aspects of the apartment industry, including ownership, development, management and finance. NMHC represents the principal officers of the apartment industry's largest and most prominent firms. As a federation of 149 state and local affiliates, NAA encompasses over 93,000 members representing more than 10.5 million apartment homes globally.

² <https://www.weareapartments.org/>

³ U.S. Census Bureau, Various Surveys.

⁴ Hoyt Advisory Services; NMHC and NAA, "U.S. Apartment Demand – A Forward Look", May 2017.

⁵ U.S. Census Bureau, New Residential Construction, updated 4/2021.

The multifamily industry has long been at the forefront of addressing housing affordability. NMHC published its Housing Affordability Toolkit with HR&A Advisors in 2018 with the goals of both providing background on the underlying causes of the apartment industry's affordability crisis and providing specific tools that could be used to help defray the cost of building new apartments, allowing more units to be built at a variety of price points.⁶

We cited three main reasons for the worsening affordability conditions: (1) a chronic demand/supply imbalance; (2) a rise in the "lifestyle" renter (or renter by choice); and (3) an increase in overall development costs including materials and regulatory compliance. Together, these factors created a scenario that put the brakes on affordable housing production. It became increasingly challenging to buy land and build a property at rates that were broadly affordable. Furthermore, it was exceedingly difficult for lower-income renter households to find an apartment without becoming cost-burdened. In the time since the publication of the Affordability Toolkit, there has been a pandemic-induced economic downturn, one that put lower-income apartment residents particularly at risk financially.⁷

The multifamily industry wishes to work with Congress and the Biden Administration to address these challenges. To this end, we strongly urge Congress to pass a comprehensive infrastructure plan that reinvests in America's infrastructure, creates good-paying jobs and addresses the nation's pressing housing needs. Put simply, housing is infrastructure. Moreover, both the existing supply of apartments and new apartment development are directly dependent on the condition and availability of suitable transportation options, reliable water and utility infrastructure, and broadband and telecommunications services. Successful new housing development relies on sustained funding for infrastructure and the modernization of infrastructure assets.

The House of Representatives recognized these synergies last Congress when it passed H.R. 2, the *Moving Forward Act*. We urge Congress to build on that legislation in a bipartisan manner and swiftly enact legislation that takes a broad and cooperative approach to housing development and infrastructure planning.

As the House Ways and Means Committee and Congress consider infrastructure initiatives, we urge the inclusion of the following measures within the Committee's jurisdiction that support the interconnectivity between housing and infrastructure and promote housing development at all income levels, including:

- Expanding and enhancing the Low-Income Housing Tax Credit;
- Enacting the Middle-Income Housing Tax Credit to support workforce housing;
- Enhancing Opportunity Zones to incentivize the rehabilitation and preservation of multifamily buildings;
- Promoting the rehabilitation of multifamily housing located near transit;
- Supporting measures to help property owners retrofit properties to meet building performance goals in line with our national climate policy.

Each of these proposals is briefly described in the pages that follow, and we note that many have bipartisan support.

While history has shown us that investment in infrastructure stimulates the economy, we understand that the House Ways and Means Committee is charged with finding the resources necessary to finance legislation. NMHC and NAA have serious reservations regarding revenue-raising proposals that would seek to restrict the scope of tax policies that currently underpin housing production. Even with beneficial tax provisions, affordable housing production has encountered strong headwinds. Limiting or eliminating these tools (as discussed below to offset the cost of a large infrastructure

⁶ <https://housingtoolkit.nmhc.org/>

⁷ <https://www.nmhc.org/research-insight/research-notes/2020/which-apartment-residents-are-most-affected-by-job-losses/>

package will certainly have an adverse effect on new housing production and the necessary rehabilitation of older housing stock. If enacted, these proposals would inhibit the capital flows that are so critical to the development and preservation of multifamily housing units. In so doing, they would make the production and development of multifamily housing more costly and further exacerbate our housing affordability challenges. In particular, the multifamily industry opposes the Biden Administration's proposals to:

- Limit the deferral of gain from like-kind exchanges;
- Increase capital gains tax rates;
- Tax unrealized capital gains at death; and
- Tax carried interest as ordinary income.

The final portion of this statement discusses each of these proposals that we urge Congress to reject.

PROPOSALS TO SUPPORT THE DEVELOPMENT AND PRESERVATION OF MULTIFAMILY HOUSING

Housing production is not a zero-sum game; we need to produce housing at prices that are broadly affordable across the income spectrum. Our nation's supply of multifamily properties is aging. In fact, 76 percent of apartment properties are more than 20 years old.⁸ If we look at apartment buildings with 50 or more units, we find that 44 percent of those units were built in 1979 or earlier.⁹ The country must build 328,000 new apartment homes each year to meet projected demand by 2030.¹⁰ The industry has only hit that mark four times since 1989.¹¹ To address housing production and preservation, we recommend Congress enact the following policies:

Expand and Enhance the Low-Income Housing Tax Credit

The Low-Income Housing Tax Credit (LIHTC) is a public/private partnership that leverages federal dollars with private investment to produce affordable rental housing and stimulate new economic development in many communities. Since its inception in 1986, the LIHTC program has according to the A Call To Invest in Our Neighborhoods (ACTION) Campaign financed 3.5 million apartments and served 8 million households. The LIHTC program provides critical support to the nation's affordable housing production but could be made even more impactful.

NMHC and NAA strongly support the ***Affordable Housing Credit Improvement Act of 2021 (H.R. 2573/S. 1176)***. Introduced by House Ways and Means Committee Members Suzan DelBene, Jackie Walorski, Don Beyer, and Brad Wenstrup (and cosponsored by other committee members), this bipartisan bill would, among other provisions, make permanent the increased LIHTC credit authority enacted in March 2018 to enable the production of new units and further augment credit authority by 50 percent. The ACTION Campaign estimates this legislation would "result in the production of over 2 million additional affordable homes over the next decade, support the creation of nearly 3 million jobs, and generate more than \$346 billion in wages and business income and nearly \$120 billion in additional tax revenue."¹²

Enact the Middle-Income Housing Tax Credit (MIHTC) to Support Workforce Housing

Housing affordability is an issue threatening the financial wellbeing of solidly middle-income households in addition to low-income families. Consider that the Joint Center for Housing Studies of

⁸ <https://weareapartments.org/>

⁹ NMHC analysis of American housing Survey

¹⁰ <https://weareapartments.org/>

¹¹ US Census Bureau, New Residential Construction, updated 4/2021.

¹² <https://static1.squarespace.com/static/566ee654bfe8736211c559eb/t/6079f11458d2131df3c32c12/161860431029/9/AHCIA+One+Page+Summary+-+April+2021+-+Final.pdf>

Harvard University found in its *America's Rental Housing 2020* report that the median asking rent for an apartment constructed between July 2018 and June 2019 was \$1,620.¹³ For a renter to afford one of those units at the 30 percent of income standard, they would need to earn at least \$64,800 annually. Accordingly, this is an issue impacting those workers who comprise the very fabric of strong communities nationwide, including teachers, firefighters, nurses and police officers.

Tax policies to spur the production of multifamily housing targeted to middle-income Americans should be a part of any infrastructure bill. We urge Congress to strongly consider the **Middle-Income Housing Tax Credit Act of 2018** (S. 3365) that was introduced by Senate Finance Committee Chair Ron Wyden during the 115th Congress to address the shortage of workforce housing available to American households. A worthy complement of measures to expand and improve LIHTC, the Middle-Income Housing Tax Credit (MIHTC) takes over where LIHTC leaves off. LIHTC is currently designed to serve populations of up to 60 percent of area median income. MIHTC is designed to benefit populations earning below 100 percent of area median income.

Enhance Opportunity Zones to Incentivize Rehabilitation of Housing Units

Enacted as part of tax reform legislation in 2017, Opportunity Zones are designed to provide tax incentives for investments in distressed communities. Opportunity Zones hold great promise for the development of multifamily housing. Under the new program, Governors have designated over 8,700 qualified low-income census tracts nationwide as Opportunity Zones. Up to 25 percent of a state's qualified census tracts may qualify as Opportunity Zones, with each state having to designate a minimum of 25 Zones.

While we expect the Opportunity Zones program to be beneficial in spurring the production of new multifamily housing, the program could be improved with respect to incentives for the rehabilitation and preservation of existing multifamily units. Current regulations work against using this program to rehabilitate properties for affordable housing since the developer must double her basis in the property without consideration of the cost of land. In many cases, such significant renovation is unnecessary to preserve buildings and units that might otherwise be lost to obsolescence. Congress could leverage the Opportunity Zones program to promote the rehabilitation and preservation of multifamily units and, thereby, positively address the shortage of apartment units.

NMHC and NAA recommend that Congress consider statutory modifications to reduce the basis increase necessary to qualify a multifamily rehabilitation project for Opportunity Zone purposes. It is noteworthy that to qualify for an allocation under the LIHTC, owners must commit to rehabilitations valued at the greater of: (1) 20 percent of adjusted basis of a building; Or (2) \$6,000 (\$7,100 in 2021 as adjusted for inflation) per low-income unit.

Promote the Rehabilitation of Multifamily Housing Located Near Transit

NMHC and NAA strongly support bipartisan legislation that would provide a new tool aimed at encouraging greater community development and inclusive neighborhood revitalization. Introduced by House Ways and Means Committee member Earl Blumenauer and cosponsored by committee members Mike Kelly, Dan Kildee, and Darin LaHood, the **Revitalizing Economies, Housing and Business Act (REHAB Act)** (H.R. 1483) provides:

- a 15 percent tax rehabilitation credit for buildings that are more than 50 years old, not certified historic structures, and are within one-half of a mile of a public transportation station;
- expanded credit eligibility to include building expansion on the same block; and
- a bonus credit of 25 percent for expenses related to public infrastructure upgrades and rent-restricted housing.

¹³ Joint Center for Housing Studies of Harvard University, *America's Rental Housing 2020*, pg. 2.

Strengthen Communities through Policies that Support Resiliency

Building utility costs are second only to debt service in terms of property expenses. Efficient use of resources, including updating building systems and appliances, is key to ensuring that housing remains affordable for residents. The multifamily industry has a long history of support for building-performance benchmarking and water and energy conservation and favors incentive-based strategies that improve building energy performance and community-wide resiliency efforts.

Building performance standards that overlook the age of the existing apartment stock and fail to consider the inherent efficiencies of compact development that is the hallmark of multifamily design buildings will exacerbate the shortage of affordable apartment units. Policies that provide financial assistance for owners to reinvest in higher-performing building systems and components outside of replacement *pro formas* will be critical to advancing building performance goals. Layering additional conditions on these investments, including requirements about the workforce that must be employed to make these renovations, will eliminate the utility of the efficiency incentives that have been available under Sec. 45 L or Sec. 179D.

As Congress considers legislation to promote resilience and reduce greenhouse gas emissions across the economy, programs that address building energy performance are an essential element. Policymakers should resist applying one-size-fits-all efficiency mandates that will exacerbate the shortage of affordable housing in the near term. Incentives that enable developers to invest in engineering, construction and development costs that are required to build/rehab multifamily apartment homes will speed the development of higher-performing, more resilient housing that is affordable for renter households.

Make Permanent the New Energy Efficient Homes Credit (Sec. 45L): This tax credit has provided a necessary incentive for builders of apartment buildings (3 stories or fewer) to install higher performance building systems and upgraded appliances than they otherwise could justify within the pro forma for developing the property. While this credit has been extended through 2021, it should be made permanent as an essential part of a national plan to boost production of high-performance buildings and reduce greenhouse gas emissions.

Improve the Energy Efficient Commercial Buildings Deduction (Sec. 179): This tax deduction has primarily been used to encourage energy-efficient new construction. However, since 179D's initial enactment in 2005, the intent has also been to encourage private-sector and non-profit owners to retrofit existing buildings. In this regard, Sec. 179D can be improved. Considering the age of current high-rise apartment building stock, Sec. 179D should be strengthened to encourage retrofits and, thereby, maximize the incentive's potential as an engine for sound tax, jobs, energy, and environmental policy. Title I of the ***Energy Efficiency Tax Incentives Act*** (S. 2189), introduced by Senators Ben Cardin, Dianne Feinstein, and Brian Schatz in the 113th Congress, preserves the deduction's application for new construction and public buildings, while also meaningfully incentivizing private-sector and non-profit retrofits.

TAX PROPOSALS THAT WOULD INHIBIT THE DEVELOPMENT AND PRESERVATION OF MULTIFAMILY HOUSING

NMHC and NAA believe that tax policy should not inhibit the capital flows that underpin the multifamily industry's ability to develop and preserve units. We have serious reservations regarding the Biden Administration's revenue-raising proposals below that would have an adverse effect on new housing production and the necessary rehabilitation of older housing stock. As Congress drafts new tax laws, the multifamily industry recommends that policymakers oppose the Biden Administration's proposals to:

Limit the Deferral of Gain from Like-Kind Exchanges

Ensuring the nation has a sufficient supply of quality affordable housing is an important public policy goal, and one that is pursued through housing and tax policy. One way tax laws support investment in real estate is through Section 1031 like-kind exchanges.

Retained for real property as part of the *Tax Cuts and Jobs Act* enacted in late 2017, like-kind exchange rules encourage investors to remain invested in real estate by allowing property owners to defer capital gains tax if, instead of selling their property, they exchange it for another comparable property. As long as the taxpayer remains invested in real estate, tax on any gain is deferred. When the taxpayer ultimately does sell the asset, the property tax is paid.¹⁴ Notably, taxpayers utilizing like-kind exchanges carry over the basis of the original property to the acquired property, thereby losing the ability to take depreciation at the higher exchange value. Section 1031 is one of many non-recognition provisions in the Code that provide for deferral of gain.¹⁵

While Congress eliminated like-kind exchanges for personal property as part of the *Tax Cuts and Jobs Act*, it sensibly retained like-kind exchanges for real property. Unfortunately, the Biden Administration is now proposing to limit gain deferral from like-kind exchanges to \$500,000 for single taxpayers and \$1 million for married taxpayers.

Like-kind exchange rules play a crucial role in supporting the multifamily sector by encouraging investors to remain invested in real estate while still allowing them to balance their investments to shift resources to more productive properties, change geographic location, or diversify or consolidate holdings. In addition, without like-kind exchanges, property owners are deterred for tax reasons from selling assets that are in need of capital investment. Exchange rules allow those owners to transfer the property to new owners who can invest the necessary capital to revitalize the asset. Thus, like-kind exchange rules facilitate job-creating property upgrades and improvements.

According to recent research by Drs. David C. Ling and Milena Petrova regarding the economic impact of repealing like-kind exchanges for real estate and the multifamily industry,¹⁶ in the absence of like-kind exchanges and assuming no state income taxes, after-tax apartment rental income would have to increase by between 0.44 percent and 9.29 percent with a mean value of 4.66 percent. Alternatively, mean market asset prices would have to decline by these amounts to offset the impact of like-kind exchange elimination. Notably, Ling and Petrova draw the following conclusion regarding like-kind exchanges:

We conclude that elimination of real estate exchanges would likely lead to a decrease in transaction activity in most CRE markets as well as price declines in some markets,

¹⁴ The like-kind exchange rules are based on the concept that when one property is exchanged for another property, there is no receipt of cash that gives the owner the ability to pay taxes on any unrealized gain. The deferral is limited to real property and does not extend to investments that are liquid and readily convertible to cash, such as securities. Furthermore, the person who exchanges one property for another property of like-kind has not really changed his economic position; the taxpayer, having exchanged one property for another property of like-kind is in a nearly identical position to the holder of an asset that has appreciated or depreciated in value, but who has not yet exited the investment.

¹⁵ Under the tax code, the mere change in value of an asset, without realization of the gain or loss, does not generally trigger a taxable event. In such situations, the proper tax treatment is to defer recognition of any gain and maintain in the new property the same basis as existed in the exchanged property. This is similar in concept to other non-recognition, tax deferral provisions in the tax code, including property exchanges for stock under Section 351, property exchanges for an interest in a partnership under section 721, and stock exchanges for stock or property under section 361 pursuant to a corporate reorganization.

¹⁶ David C. Ling and Milena Petrova, *The Tax Economic Impacts of Section 1031 Like-Kind Exchanges in Real Estate*, October 2020.

at least in the short run. These price declines would be more pronounced in states with high income tax rates. Elimination would also likely produce a decrease in capital investment on acquired properties, an increase in investment holding periods, and an increase in the use of leverage to finance acquisitions. Overall, our analysis suggests the cost of like-kind exchanges to the U.S. Treasury is likely overestimated, while their benefits to smaller investors and to local CRE markets are often overlooked.

Finally, additional research completed by EY illustrates the significant economic activity like-kind exchanges support. Indeed, EY finds that in 2021, like-kind exchanges support 568,000 jobs, \$27.5 billion in total labor income, and \$55.3 billion in total value-added economic activity.¹⁷

Increase Capital Gains Tax Rates

The Biden Administration is proposing to increase the top long-term capital gains rate to 39.6 percent to the extent a taxpayer's income exceeds \$1 million. This would equalize the top tax rates applicable to ordinary income and long-term capital gains income. When the 3.8 percent net investment income tax is considered, the top tax rate on long-term capital gains would be 43.4 percent.

NMHC and NAA believe that long-term capital gains should be taxed at lower rates than ordinary income to account for the significant entrepreneurial risk developers take when they forego a guaranteed salary to begin the complex and time-consuming pre-development/development phase of multifamily property. The industry is concerned that developers may decide to take fewer risks if capital gains rates rise to a level of 43.4 percent. This would lead to fewer multifamily housing units. Additionally, a lower capital gains rate helps to compensate for gains attributable purely to inflation as opposed to real returns. For example, if an asset rises 50 percent in value after being held for 10 years and the annual rate of inflation is 2 percent, inflation alone would represent 43.8 percent of the total gain (inflation would be 21.9 percent on a cumulative basis). While taxpayers are today taxed on that inflationary gain, tax rates on such gain should not be raised to 43.4 percent.

Congress has long recognized that a differential between ordinary income and long-term capital gains rates can stimulate economic activity. Indeed, in the 108 years since Congress enacted the modern Federal income tax in 1913, there has been a lower long-term capital gains tax rate in 105 of those years. In just three years – those following the enactment of the *Tax Reform Act of 1986* – did the top ordinary income tax rate equal the top long-term capital gains tax rate.

Tax Carried Interest as Ordinary Income

A carried interest, also called a “promote,” has been a fundamental part of real estate partnerships for decades. Investing partners grant this interest to the general partners to recognize the value they bring to the venture as well as the risks they take. Such risks include responsibility for recourse debt, litigation risks and cost overruns, to name a few.

Current tax law treats carried interest as a long-term capital gain if the underlying asset is held for at least three years. The multifamily industry strongly opposes the Biden Administration's proposal to tax carried interest at ordinary income tax rates to the degree a taxpayer's income exceeds \$400,000. Additionally, we object to the *Carried Interest Fairness Act of 2021* (H.R. 1068) introduced by House Ways and Means Oversight Subcommittee Chair Bill Pascrell.

Carried interest should receive capital gains tax treatment because it represents a return on an underlying, long-term capital asset, as well as risk and entrepreneurial activity. This is in contrast to any fees that managing partners receive in payment for operations and management activities, which are taxed as ordinary income.

¹⁷ EY, *Economic contribution of the like-kind exchange rules to the US economy in 2021*, May 2021.

A higher tax rate on long-term capital gains will discourage real estate partnerships from investing in new construction at a time when demand for apartments continues to grow and chronic underbuilding has limited new housing supply. Furthermore, such a reduction would translate into fewer construction, maintenance, on-site employee, and service provider jobs.

Tax Unrealized Capital Gains at Death

The Biden Administration proposes to tax unrealized capital gains at death for certain taxpayers. There would be an exclusion of up to \$2.5 million exclusion per couple where part of the unrealized gain is on a principal residence. Additional rules would defer taxes until sale to protect heirs who continue to run family-owned businesses from having to sell the property to pay the tax. The proposal would also allow taxes to be paid over 15 years with respect to appreciated assets transferred at death except liquid assets or those for which deferral is elected pursuant to rules applicable to family-owned businesses. Notably, House Ways and Means Oversight Subcommittee Chairman Bill Pascrell has also introduced legislation, H.R. 2286, to address this area of the tax law.

While the Biden Administration's proposal is specifically analyzed below, the taxation of unrealized capital gains at death, if enacted, would have extremely negative consequences for taxpayers, the real estate industry, and the economy.

Effect on Taxpayers. At the taxpayer level, death would become a taxable event at \$1.25 million for single filers with a primary residence (assuming there is at least \$250,000 of unrealized gain in the home) and at \$2.5 million for married taxpayers with a primary residence (if there is at least \$500,000 of gain in the home). In contrast, the estate tax is imposed at far higher asset levels (\$11.7 million for single filers and \$23.4 million for married filers). The last year estate taxes were imposed at an asset level of less than \$1.25 million for a single filer or \$2.5 million for a married filer was 2003. There is little reason to make death a taxable event at the lower asset levels contemplated by the Biden Administration.

As described above, the Biden Administration also includes a proposal to nearly double the capital gains tax rate for those with income above \$1 million per year. When combined with the net investment income tax of 3.8 percent, which the Biden Administration also proposes to apply to more taxpayers, the top rate would be 43.4 percent, not including any state tax.

It should be noted that for taxpayers subject to both the taxation of unrealized gains at death at this new top rate of 43.4 percent and the estate tax, the combined marginal tax rate would rise from the top current law estate tax rate of 40 percent to 66.04 percent, assuming that the tax on unrealized capital gains were deductible from the estate tax. The last time estates were taxed at such high levels was for decedents dying in 1981.

Effect on Real Estate Industry. The Biden Administration's proposal could have extraordinarily negative consequences for the apartment industry and the preservation of affordable housing, in particular. While heirs not inheriting a family-owned business would have 15 years to pay taxes due, the annual installment could represent a sizable percentage of the asset's annual underlying operating income. Moreover, taxes on current-year operating income would still apply. In sum, once all taxes are paid, there might be little left over to maintain and upgrade the property.

Consider the following example to illustrate this point: Robert, a single individual, acquired a 25 percent partnership interest in an apartment development with 720 units in 1995 for \$6 million before passing away in 2022, leaving the property to his nephew, Eric. At the time of Robert's death, the property is worth \$64 million (Robert's share is \$16 million) and, due to depreciation of \$26 million (Robert's share is \$6.5) million and improvements of \$10 million (Robert's share is \$2.5 million), has a tax basis of \$8 million (Robert's tax basis is \$2 million). The property has annual operating net

income of \$4.48 million (Robert's share is \$1.12 million). Assume this is the only capital asset in Robert's estate. However, Robert also has unrelated debts of \$7 million.

Under current law, Robert would not owe estate tax, as he would be under the exemption level. When Eric inherits his partnership interest in the apartment development, the \$2 million in tax basis would be stepped-up to \$16 million. Tax would only be imposed when Eric disposes of his partnership interest and would be based on the difference between the value of the partnership interest at time of sale and the \$16 million in tax basis (plus any post-inheritance adjustments).

Under the Biden Administration's proposal, Robert's estate would recognize a capital gain of \$13 million. (This is calculated as \$16 million in fair market value, less \$2 million in basis, less a \$1 million exclusion). This capital gain would be taxed at 43.4 percent given the Biden Administration's proposals to: (1) tax capital gains at ordinary income rates (39.6 percent) for taxpayers earning over \$1 million; and (2) impose the 3.8 percent net investment income tax on all trade or business income not otherwise subject to employment taxes for taxpayers earning more than \$400,000. Robert's capital gains tax liability would thus total \$4.446 million. (This is calculated as $.434$ (capital gains tax rate \times \$6.5 million) + $.25$ (depreciation recapture rate) \times \$6.5 million).

While the \$4.446 million capital gains tax can be paid over 15 years, the annual tax due would be \$296,400. This would represent 26.5 percent of Eric's share of the partnership's net income. Of course, tax would also be due on the net operating income flowing to the partnership interest. On a combined basis, Eric might have little left over to make significant capital improvements in the underlying apartment development or to make other real estate investments.

Finally, as noted above, the Biden Administration would allow family-owned businesses to defer the payment of tax until an inherited asset is sold. While tax may not be immediately due, an heir could well inherit an apartment property with little or no basis and sizeable debt. If it is sold, the heir will face significant depreciation recapture taxes and capital gains taxes. This discourages heirs from investing further capital to maintain it and could also remove valuable affordable housing from inventory.

Effect on the Economy: On a macroeconomic level, an April 2021 EY study prepared for the Family Business Estate Tax Coalition estimates that imposing tax on transferred assets at death would result in 80,000 fewer jobs in each of the first 10 years and 100,000 jobs each year thereafter. Gross Domestic Product relative to the U.S. economy would also fall by \$10 billion annually and \$100 billion over 10 years. Workers' wages would plummet by \$32 for every \$100 collected in tax.¹⁸

Conclusion

Quality affordable housing in strong communities shapes the American dream. As Congress embarks on the generational effort to restore America's infrastructure, it is essential that the nation's unmet housing needs be addressed. We applaud Congressional efforts to explore this relationship and find solutions to the nation's most significant housing challenges. Policymakers at every level of government have a role to play in removing obstacles to housing production, easing costs and creating a supportive environment for the providers of apartment homes. Across all markets, the supply of multifamily rental housing at a variety of price points will play a vital role in promoting economic growth, attracting and retaining talent and encouraging household stability for all American families. Using a combination of incentive-based programs, streamlined regulatory burdens and innovative solutions, while rejecting counterproductive tax increases, we stand ready to work with Congress and the Administration to address the housing affordability challenges faced by communities across the nation while making critical investments in infrastructure of all types.

¹⁸ EY, *Repealing step-up of basis on inherited assets: Macroeconomic impacts and effects on illustrative family businesses*, April 2021.