TAX CUTS & JOBS ACT

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Tax reform has capacity to reshape the multifamily industry.

Reform can impact taxes paid at all stages of development:
- Building
- Operating
- Sale
- Transfer to Heirs

NMHC supports reform that promotes economic growth and investment in multifamily housing.
TAX REFORM – KEY MULTIFAMILY ISSUES

- Protect Flow-Through Entities / REIT Structure
- Retain Full Business Interest Deduction
- Ensure Depreciation Rules Avoid Harming Real Estate
- Maintain Like-Kind Exchanges for Real Property
- Preserve Carried Interest
- Maintain Estate Tax and Basis Step-Up
- Preserve the Low-Income Housing Tax Credit
TAX CUTS & JOBS ACT

- Signed into law on December 22, 2017
- Impacts all of NMHC’s Key Issues
- Provisions Generally Effective in 2018
- Key Tax Reduction Provisions for Multifamily Sunset in Many Cases (e.g., after 2025)
TAX RATES

Prior Law Tax Rates
- Flow-through entity: 39.6 percent max rate
- Individual: 39.6 percent max rate (effective at $418,400 single filers / $470,700 married couples)
- REIT: 39.6 percent max rate on dividends
- Corporate: 35 percent max rate

Tax Cuts & Jobs Act
- Individual: 37 percent max rate (effective at $500,000 individuals / $600,000 married couples) (through 2025)
- Flow-through entity: 20 percent deduction (29.6 percent max rate) for qualifying business income (through 2025)
- REIT: 20 percent deduction for REIT dividends (through 2025)
- Corporate: 21 percent max rate (permanent)
TAX RATES – THE 20% DEDUCTION

Flow-through entity 20 percent deduction mechanics

- For taxpayers earning over $157,500 (single filers) and $315,000 (married couples), deduction is limited to greater of:
  1. 50% of the taxpayer’s share of aggregate W-2 wages paid by the business; OR
  2. 25% of the taxpayer’s share of aggregate W-2 wages paid by the business plus 2.5% of the unadjusted basis, immediately after acquisition, of all qualified property (i.e., structures but not land).

- Applies only to property held at the end of a taxable year.
- Deduction applies at the trade or business level.
  - NMHC supports allowing grouping of multiple partnerships into a single trade or business.
- Income from trusts and estates and REIT dividends eligible.
  - REIT deduction must be clarified to allow shares held by mutual funds to qualify.
TAX RATES – THE 20% DEDUCTION

Scenario: A multifamily firm purchases an apartment building for $20 million ($14 million attributable to the structure, $6 million attributable to the land). The building generates net annual income of $1.25 million.

Maximum Deduction Before Limitation: The maximum pass-through deduction would be $250,000 (20% of $1.25 million).

Deduction Limitation Calculation: The deduction would be limited to 2.5 percent of unadjusted basis (i.e., 2.5 percent of $14 million), or $350,000.

Maximum Deduction Available to Taxpayer: The taxpayer gets the full deduction of $250,000, regardless of the wage limitation.
DEDUCTIBILITY OF BUSINESS INTEREST

Prior Law
- Business interest fully deductible.

Tax Cuts & Jobs Act
- Imposes limitation on business interest (exempts firms with less than $25 million in average annual gross receipts over past three years).
- Real estate companies may elect to maintain full deductibility of interest.
- Election requires longer depreciation period for buildings.
DEPRECIATION

■ Prior Law
  - Depreciation of Residential Structures: 27.5 years.
  - Depreciation of Tangible Personal Property: Bonus depreciation through 2019 / MACRS thereafter.

■ Tax Cuts & Jobs Act
  - Depreciation of Residential Structures: 30 years if electing out of limits on interest deductibility, otherwise 27.5 years.
  - Statute could be read to require 40 years for existing structures for firms electing out of interest.
    - NMHC is asking Treasury to clarify existing structures should be depreciated over 30 years.
  - Depreciation of Tangible Personal Property:
    1. Full expensing through 2022.
    2. Bonus depreciation thereafter through 2026 (80% in 2023, 60% in 2024, 40% in 2025, and 20% in 2026).
LIKE-KIND EXCHANGES

- Prior Law
  - Like-Kind Exchanges: Available for all property held for investment or use in a trade or business.

- Tax Cuts & Jobs Act
  - Like-Kind Exchanges: Limited to exchanges of real property.
CARRIED INTEREST

Prior Law
- Carried Interest: Eligible for capital gain if asset held for at least one year.

Tax Cuts & Jobs Act
- Carried Interest: Eligible for capital gain if asset held by partnership and partnership interest held by partner for at least three years.
ESTATE TAX

Prior Law
- Exemption: $5.49 million individual / $10.98 million married couple
- Top Rate: 40%
- Basis Rule: Step up

Tax Cuts & Jobs Act
- Exemption: Doubled in 2018 (reverts to prior law in 2026)
- Top Rate: 40%
- Basis Rule: Step up
LOW-INCOME HOUSING TAX CREDIT

Prior Law

- LIHTC in law to help finance affordable units.
- Private Activity Bonds support LIHTC.

Tax Cuts & Jobs Act

- LIHTC and Private Activity Bonds retained as under prior law.
- Lower corporate tax rate and chained CPI could lead to loss of 235,000 affordable units over next 10 years (Novogradac and Company LLP).
- Recent Legislation: 12.5% Credit Increase (2018-2021) & Income Averaging
ACTIVE LOSSES

Prior Law

- Active business losses fully deductible against active business income.

Tax Cuts & Jobs Act

- Deduction of net active pass-through losses against wage or portfolio income limited to $500,000 (married filers) and $250,000 (single filers).
- Disallowed losses may be carried forward as part of a taxpayer’s net operating loss.
- Provision effective through 2025.
DEVELOPMENT INCENTIVES

- Prior Law Granted Two Other Development Incentives:
  - New Markets Tax Credit (effective through 2019).
  - Historic Rehabilitation Tax Credit.

- Tax Cuts & Jobs Act
  - New Markets Tax Credit retained as under current law.
  - The 20% historic credit is retained but spread over five years.
  - The 10% credit for pre-1936 non-historic buildings is repealed.
  - Opportunity Zones for Capital Gains Deferral
    - Deferral of gains invested in Opportunity Fund to as late as 2026
    - No tax on Opportunity Fund gains held at least 10 years
NMHC will seek to ensure regulations implementing the provisions operate as Congress intended.

NMHC will look to make permanent beneficial tax provisions that expire.

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