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 Committee's May 16, 2018, hearing titled *Tax Reform: Growing Our Economy and Creating Jobs*.

For more than 20 years, NMHC and NAA have partnered 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 160 state and local affiliates, NAA encompasses over 75,000 members representing 9.25 million rental housing units globally.

At the outset, we would like to take this opportunity to congratulate Congress for enacting landmark tax reform legislation that we believe holds great promise for generating economic growth and fostering job creation. As multifamily housing firms begin to implement the new tax law, we want to draw your attention to several provisions that we request Congress and the Treasury Department work together to clarify so that our industry can build the 4.6 million new apartment units our nation needs by 2030. Without tax certainty, we are concerned that capital could sit on the sidelines and not be fully deployed.

Depreciation Period of Existing Multifamily Buildings

Our first request is that Congress either enact a technical correction or work with the Treasury Department to issue guidance to clarify that multifamily buildings in existence prior to 2018 be depreciated over 30 years for firms that elect out of limits on interest deductibility.

By way of background, Section 13204 of the tax reform law ("Applicable Recovery Period for Real Property") reduces the recovery period for residential rental property from 40 to 30 years for purposes of the alternative depreciation system (ADS) and requires real estate firms electing out of the limits on interest deductibility of Section 163(j) to use ADS to depreciate multifamily buildings. While we believe that Congress' intent was to apply this 30-year period to multifamily buildings in existence before enactment of the tax law and those yet to be placed in service, we are extremely concerned that without clarification, the statute requires that multifamily properties in existence prior to 2018 be depreciated over 40 years with regard to their remaining life.

The confusion arises because the interest deduction limitation rules are based on taxable year concepts and have an effective date of taxable years beginning after 2017, while the effective date for the ADS recovery period change is based on a placed-in-service concept (as depreciation changes generally are). It is the combination of two different types of effective dates in section 13204(b) of the statute that gives rise to the confusion.

We believe that Congress did not intend for existing multifamily buildings to be depreciated over 40 years for real estate firms electing out of interest deductibility limits. Reading the statute to require existing buildings to be depreciated over 40 years is unlikely to reflect Congress' intent from a policy perspective. There are few policy arguments for requiring real estate firms electing out of interest deductibility limits to depreciate buildings in existence prior to 2018 over 40 years instead of the previously applicable 27.5 years while allowing only new buildings to be depreciated over 30 years. Congress seems unlikely to have consciously wished to make such a drastic change.

Congress can be a key player in enabling existing multifamily properties to be depreciated over 30 years by enacting a technical correction or encouraging the Treasury Department to issue guidance. We believe Treasury can address this issue through the regulatory process either using the broad authority provided in IRC Section 163(j)(7) that addresses how real property trades or businesses elect out of limits on interest deductibility or under the "change of use authority" of IRC Section 168(i)(5).

Section 163(j) as amended by the tax reform law generally limits a taxpayer's allowable deduction for business interest. The legislation, however, enables real property trades or businesses to elect out of the limitation and requires that "Any such election shall be made at such time and in such manner as the Secretary shall prescribe, and, once made, shall be irrevocable." One consequence of making the election is that real property trades or businesses must depreciate real property using ADS.

We believe that the "in such manner" language provides the Treasury Department with sufficient authority to allow electing real property trades or businesses to use post-enactment ADS (i.e., the 30-year life) for purposes of depreciating multifamily property. In other words, Treasury can allow real estate firms to make the option of interest deductibility limitation *in such manner* that requires a 30-year ADS life.

In addition, the legislative history makes it clear that Congress intended that the election out of the interest limitation and the required use of ADS be treated as a change in use of the property. (Footnote 455 of the Senate Finance Committee report). Treasury has broad authority under section 168(i)(5) to provide rules to implement changes in use of depreciable property, including rules to provide when such property is deemed placed in service.

In sum, we ask that Congress either enact a technical correction or encourage the Treasury Department to issue guidance that would enable real estate firms that elect out of the interest limitation to depreciate multifamily property in existence prior to 2018 over a 30-year ADS schedule. A failure to swiftly take action will unnecessarily disrupt cash flows and increase the tax liability of multifamily firms, reducing their ability to invest in their assets or develop new properties. That result would be contrary to the goal of the tax reform bill, and we ask that it be avoided.

Pass-Through Tax Deduction for Qualified Business Income

The multifamily industry is also eagerly awaiting guidance regarding the 20 percent deduction for pass-through income under new IRC Section 199A. We believe that if properly implemented, this provision has the potential to unleash significant investment and job creation in the multifamily industry.

As the Treasury Department drafts implementing guidance, we would encourage Congress to request the Treasury Department to address three aspects of the pass-through tax deduction:

First, the new law requires that the pass-through deduction be determined for each qualified trade or business, but it does not provide a definition of trade or business. We request that the Treasury Department issue guidance enabling individuals to aggregate or group all qualified business activities at the partner level in a manner consistent with IRC Section 469. This would help ensure entities can focus on their business activities rather than engaging in costly restructuring efforts. Additionally, we would ask that Treasury specifically allow income earned from the development, operation and management of real estate assets to qualify for the deduction.

Second, the Treasury Department should provide rules regarding the unadjusted basis of property acquired pursuant to a like-kind exchange. Such basis should be no less than the unadjusted basis of the property relinquished in the exchange plus any cash or other consideration provided in the exchange. Taxpayers engaging in like-kind exchanges remain fully invested in real estate and should not be negatively impacted when they reallocate a portfolio. Indeed, providing onerous rules regarding the unadjusted basis for exchange property would reduce the velocity of real estate transactions and amount of aggregate investment in the sector.

Third, the new law allows REIT dividends to fully qualify for the 20 percent deduction. Treasury, however, should clarify that shareholders who invest in a REIT through a mutual fund are eligible as well. Approximately half of REIT shares are held in mutual fund portfolios.

Finally, the new and novel pass-through deduction is likely to lead to further questions and concerns being raised. We look forward to working with Congress and the Treasury Department on additional matters related to the provision as the regulatory process moves forward to ensure this deduction is as effective as possible.

Deductibility of Business Interest

NMHC/NAA were most grateful that lawmakers enabled real estate firms to elect to fully deduct business interest. Given that a typical multifamily deal can be 65 percent debt financed and that the Federal Reserve reports that as of the end of 2017, there was $1.31 trillion in outstanding multifamily mortgage debt, implementation of this provision will be critical. We ask that Congress encourage the Treasury Department to quickly clarify that a taxpayer may use any reasonable allocation method to deduct business interest attributable to a real property trade or business and that debt to capitalize such enterprises is fully deductible. Our goal is to avoid any disruption to the multifamily industry that relies so heavily on debt-financed capital.

Opportunity Zones

NMHC/NAA commend lawmakers for establishing Opportunity Zones as part of the new tax law. By providing for the deferral of capital gains invested in Opportunity Funds and eliminating tax on certain gains realized from Opportunity Fund investments, there is a strong potential to drive considerable investment in multifamily housing and workforce housing, in particular, in Opportunity Zones.

We ask that Congress work with the Treasury Department to make the Opportunity Zones program as effective as possible and that lawmakers encourage the Treasury Department to ensure:

- Multifamily housing is a qualified investment for Opportunity Funds;
- Multifamily properties receiving other tax benefits, including Low-Income Housing Tax Credits, Historic Tax Credits and New Markets Tax Credits, that are necessary to make a development viable are qualified investments for Opportunity Funds. It is often only a combination of incentives that make the difference between a project being able to move forward as opposed to never breaking ground; and
- Properties of all sizes be able to receive Opportunity Fund financing.

NMHC/NAA thank you for considering our views. We again congratulate you on this landmark achievement and hope to work with the Ways and Means Committee to make the new tax law as successful as possible.