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TAX REFORM AND CRE – SPURRING INVESTMENT

By: Marc Ian Snyderman, Esq. and Antonella Colella, Esq., Snyderman Law Group, PC January 5, 2018

The Tax Cuts and Jobs Bill was signed into law on 22 December 2017. It's one of the most substantive changes to the tax laws passed in over 30 years. With the current administration's background in commercial real estate and understanding of the challenges in the industry, it's no surprise that certain provisions would be included that might help propel real estate development and commercial real estate transactions.

Here's a quick summary of a few of the critical pieces that affect the commercial real estate business. This isn't a full compendium or review of the bill and it's not tax advice but it will help guide you in developing some strategies to take advantage of these laws with your CPA in 2018.

LOWERED TAXES ON PASS THROUGH CORPORATIONS:

Pass-through businesses—partnerships, S-corporations, and limited liability companies—are corporate entities that allow business income to "pass-through" to the owner, thereby paying a personal income rate, as opposed to a business rate. For most this is a tax cut from 40% down to 25%. So, let's say you have a rental income entity organized as an LLC, this new regulation could be significant tax savings to you. Also, be sure to ask your accountant about the "Corker Kickback" which further amplifies this benefit through a 20% deduction subject to income thresholds.

TAX DEDUCTIONS FOR PROPERTY DEVELOPERS:

New provisions allow developers to deduct interest expenses for a variety of real estate activities, including construction, management, and property development. This should help developers free up some necessary cash to keep projects moving.

LIKE-KIND EXCHANGES (1031)

Like-kind exchanges enable owners of property to sell at a large capital gain but defer any tax as long as they use the proceeds to buy some other property. In essence, owners of commercial real estate can keep flipping the properties until they die without ever paying any capital gains tax. (And if the estate tax is abolished, the gains might go untaxed forever.)
Carried-Interest

There was lots of talk that the "carried interest" loophole would be closed for hedge fund managers. Carried interest essentially allows for taxation at lower capital gains rates rather than ordinary income rates for assets held at least one year. The new reform changes the hold period to three years but this won't affect most hedge funds as the average hold on assets is three years.

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In the real estate context, the change doesn't make much difference to investors who have a long-term hold strategy. However, for real estate investors who operate on a fix-and-flip strategy this could affect you directly.

CONCLUSIONS:

There are more aspects in this tax reform bill that are favorable to real estate investors and you should be consulting your CPA as soon as possible to start planning for 2018 if you haven't already. While every action has an equal and opposite reaction, most experts agree that these new regulations should spur additional investment in the commercial real estate sector from development through purchase of real estate for rental income purposes.

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