

WEBINAR

# Tax Impacts of the Infrastructure Bill on Real Estate

FRIDAY, OCTOBER 8, 2021

TODAY'S SPEAKERS



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WHY WE'RE HERE

# Learning Objectives

- Review latest legislative updates and proposals
- Explain their impact to the real estate sector
- Discuss what next steps you should take

THE UPDATE

# House Proposes Broad Tax Increases for Individuals and Businesses

- Latest piece of the reconciliation plan from the House Ways and Means Committee, approved as of September 13, 2021
- Creates new tax breaks for renewable energy, social safety net, infrastructure bonding and health care proposals
- Initial outline of the House tax plan includes roughly \$2 trillion in tax increases

## KEY HIGHLIGHTS

**Increase of Corporate Tax Rate to 26.5%**

**Individual Income Tax Rate Raised From 37% to 39.6%**

**Estate Tax Changes**

**Estate/Gift Valuation Changes**

**Grantor Trust Changes**

**Individual Retirement Accounts (IRA) Reforms**

**New 3% “Surtax” On Income Over \$5M**

**Expansion of the 3.8% Net Investment Income Tax**

**Increase in Capital Gains Tax Rate from 20% to 25% for Those Making Over \$400,000**

More information here: <https://www.armaninollp.com/articles/house-proposes-tax-increases-individuals-and-businesses/>



# The Impact on Real Estate

## TAX PROVISIONS

# Increase in Top Capital Gain Rate

- Proposal would increase the top capital gain rate from 20% to 25% for tax years ending after September 13, 2021
  - **Effective immediately!**
- Tax Cuts and Jobs Act (TCJA) required binding contract for property acquired after September 27, 2017 to qualify for 100% bonus depreciation

TAX PROVISIONS

# Surcharge on Taxpayer's Modified AGI in Excess of \$5M

- 3% surcharge on taxpayer's modified AGI in excess of \$5M (\$2.5M MFS) or \$100K for a trust or estate
  - **Highest tax rate = 43%**
- Applies after 12/31/21



## TAX PROVISIONS

# Expanded Scope of Net Investment Income Tax

- NIIT imposes a 3.8% Medicare income tax on net investment income (interest, dividends, capital gains, rental and royalty income, nonqualified annuities, and income from passive business activities)
- Proposed expansion of the scope of tax to cover specified income for taxpayers with greater than \$400k in taxable income (single) or \$500k (MFJ) as well as trusts and estates for income in their top tax rate
- NIIT would not be assessed on income on which FICA already is imposed
  - Subjecting all earnings from pass-through business to either the 3.8% self-employment Medicare tax or the 3.8% NIIT, regardless of whether the income is from a passive or nonpassive activity
  - **A taxpayer with MAGI over \$5M can potentially end up paying a total of 31.8% tax on capital gains or 46.4% on ordinary income**

## TAX PROVISIONS

# Significant Modifications to Carried Interest

- Increase 3-year holding period to qualify for long-term capital gain of an Applicable Partnership Interest to a 5-year holding period for any API
  - Any income with respect to an API that is a real property trade or business under the meaning in Section 469(c)(7)(C) will have a 3-year holding requirement
- Carried interest discussion draft that would eliminate the carried interest tax preference altogether, in-line with Biden tax proposal seeking to tax all carried interest as ordinary income subject to self-employment tax
- Real estate managers and sponsor can still defer taxes on their share of carried interest through a 1031 exchange transaction

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TAX PROVISIONS

# No Mention of 1031 Exchange Rules

- Biden proposal regarding 1031 exchanges was not mentioned in the W&M proposal
  - In the Biden plan, deferral of gain on 1031 exchanges would have been limited to \$500,000 for individual filers and \$1,000,000 for married filing joint filers

## TAX PROVISIONS

# Estate and Gift Tax Exemption Effective 12/31/21

- Under the 2017 TCJA, the estate and gift tax exemption was increased to \$10 million per individual, adjusted for inflation
  - Set to expire in 2026, reverting to \$5 million per individual, indexed for inflation
- Proposal would revert the exemption effective as of 12/31/21
  - The Joint Committee on Taxation estimates the exemption would be \$6.02 million in 2022

TAX PROVISIONS

# Temporary Tax-Free Conversion from S-Corp to Partnership

- Under current law, conversions of S corporations to an entity taxed as a partnership trigger a taxable event requiring gain recognition on appreciated properties
- Proposal to allow a temporary tax-free conversion from S corporation to partnership

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