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2015 brings another year of tax uncertainty for real estate owners

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2014 was a year of uncertainty in the tax area for the real estate industry. Many real estate companies operated in an environment of tax ambiguity without tax extenders and under the new repair versus capitalization regulations (otherwise known as the Tangible Property Regulations). As 2015 begins, the same uncertainty exists. Congress has set its sights on tax reform. However, no one is certain what the extent and implications of the reform will be. With the amount of uncertainty for 2015, it is better to focus on the key 2014 tax developments that will have an effect on 2015. These changes are the tax extenders, the Tangible Property Regulations and the Net Investment Income Tax.

Tax Extenders

After a year full of speculation, Congress finally passed an array of tax extenders for 2014 retroactive to January 1, 2014. The major issue related to the release was that the extenders were signed by President Obama on December 19, 2014 and expired again on January 1, 2015. This gave the real estate industry a full 12 days to use the tax extenders in any solid planning ideas.

The two most important extenders for real estate that were brought back are 50% bonus depreciation and the 15 year recovery life for Qualified Leasehold Improvements (QLHI). The 50% bonus depreciation allowed for a 50% deduction on property classed under the MACRS with a life less than 20 years, on QLHI, and on other qualified build-outs. The 15 year recovery life for QLHI allowed for a 15-year write-off of QLHI. The recovery life would have been 39 years without the extenders.

It remains to be seen if either of these will be part of Congress's new tax reform. This will have a major impact on how landlords structure tenant improvements and the amount of funding that's used for it in 2015.

Tangible Property Regulations

The new Tangible Property Regulations (TPR) rules went into effect on January 1, 2014. The new rules will have a major impact on the real estate industry going forward. While the new rules will make it more difficult to expense improvements, there are a number of taxpayer friendly opportunities that can be taken advantage of.

The new opportunities include:

* De minimus Expensing Election - Taxpayers can deduct up to $5,000 per item by preparing an Applicable Financial Statement and corresponding capitalization policy.

* Routine Maintenance Safe Harbor - Taxpayers can write off the cost of keeping building property in its ordinary, efficient operating condition, as long as it's expected to be performed more than once in 10 years.

* Disposition rules - Taxpayers can write off building structures that are replaced or destroyed.

These rules are being applied to 2014 tax returns being prepared in 2015. The disposition rules are very important to address during the preparation of the 2014 tax returns. These rules allow a one-time opportunity on the 2014 tax return to look back to previous years to write off any disposed of assets.

Net Investment Income Tax

The Net Investment Income Tax (NIIT) first applied to taxpayers in 2013. However, they felt the first effects of it in 2014 when they finally had to make the cash payments. In 2014 and 2015, many real estate professional are moving to plan around the tax. The tax, also known as the Medicare Tax, places a 3.8% tax on the net investment income of individuals, estates, and trusts who meet a certain threshold. The threshold is an AGI of $250,000 for couples who are married and filing jointly, or $200,000 for taxpayers filing as single.

The NIIT tax needs to be paid on rents other than those derived in an active trade or business and capital gains related to the sale of properties. This has a major impact on real estate professionals and investors. Many real estate professionals are making real estate professional elections to counteract the NIIT relating to rents and capital gain on the sale of property. If the taxpayer meets the requirements of a real estate professional, the income related to the activity is not subject to the NIIT. The test for qualifying for this safe harbor is complex, and requires strong record keeping.

Looking forward to the uncertainty of 2015, there is only one certainty. You should be consulting with your professional advisors to help navigate through the fog.

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