

TAX DEPRECIATION RULES

NMHC/NAA Viewpoint

Congress should reject proposals to ex-tend the 27.5-year depreciation period of multifamily buildings and increase the 25 percent depreciation recapture rate applicable to sales.

Tax depreciation rules enable multifamily developers to recover their investment, which promotes apartment construction, economic growth and job creation. Tax reform should ensure that depreciation tax rules match the economic life of assets by taking into account natural wear and tear, as well as technological obsolescence.

Today's depreciation rules affect owners of multifamily properties in two ways: First, a property owner may take an annual tax deduction so that a multifamily property is fully depreciated over a 27.5-year period. Second, once a property is sold, the gain in a building's value that is attributable to prior depreciation deductions is generally subject to a 25 percent tax known as depreciation recapture.

As policymakers consider tax reform, some have suggested extending the 27.5-year depreciation period and increasing the 25 percent depreciation recapture tax rate to raise revenue that would allow for lower general tax rates. Proponents of lengthening depreciation schedules for multifamily properties to as long as 43 years often cite studies that are 40 years to 50 years old. This is despite the fact that newer data strongly suggest that the depreciation of multifamily buildings should not be longer than the 27.5-year period allowed under current law, and possibly it should be shorter to truly reflect economic realities.

Depreciation rules that do not reflect the economic lives of multifamily buildings would result in less development and investment, reduce real estate values, and stifle industry's ability to create new jobs.

Raising taxes on depreciation recapture is also problematic and possibly counterproductive. After decades of operations, many multifamily owners have a very low tax basis in their properties. If they were to sell them, even under current law they would have to pay large depreciation recapture taxes. To avoid this tax bill many current owners will not only avoid selling their properties, but they will also be reluctant to make additional capital investments in properties with little value. The result is deteriorating properties that are lost as safe, affordable housing. Increasing depreciation recapture taxes would only make the problem worse.