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national policy
bulletin

National Association of Real Estate Investment Trusts®

CONGRESS REACHES AGREEMENT ON JOBS AND GROWTH TAX ACT

PROVIDES SOME LIMITED BENEFITS TO REITS

On May 21, 2003, House and Senate conferees announced that they had agreed on a $350 billion Jobs and Growth Tax Relief package that is expected to pass Congress prior to Memorial Day. President Bush said today that he is eager to sign the legislation.

Outline of Package

The final bill largely follows the House version of H.R. 2. It reduces the maximum individual tax rate for capital gains generally from 20% to 15% (from May 6, 2003 through 2008), and for dividends generally from 38.6% to 15% (from 2003 through 2008). It also accelerates the individual, ordinary income tax rate cuts scheduled for 2004 and 2006 to this year, including a maximum 35% tax rate. Absent future Congressional action to extend these rate cuts, the maximum tax rate on capital gains would return to 20% in 2009, and the maximum rate on dividends and ordinary income would move to 35% in 2009 (39.6% in 2011).

REITs and the 15% Rate

With respect to REITs, the legislation provides some limited benefits in connection with the capital gain and dividend provisions. Because REITs receive a dividends paid deduction that enables them to regularly bypass the corporate tax, REIT dividends are generally ineligible for the 15% dividend rate. However, the 15% tax rate will apply to: (1) capital gains on the sale of REIT stock; (2) REIT capital gains distributions (except to the extent of real estate depreciation recapture, which continues to be taxed at 25%); (3) REIT dividends attributable to dividends received by the REIT from non-REIT corporations, such as taxable REIT subsidiaries; and (4) REIT dividends to the extent attributable to income that was subject to tax by the REIT at the corporate level (*e.g.*, “built-in gains” or when a REIT distributes less than 100% of its taxable income).

REIT Improvement Act

All other extraneous provisions contained in the Senate bill, including the REIT Improvement Act (RIA), were dropped from the final legislation that ended up largely reflecting President Bush’s original agenda items and nothing else. Senator Orrin Hatch (R-UT) inserted the RIA

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into the Senate version of the bill. NAREIT anticipates Senator Hatch now will introduce the RIA in the Senate after the Memorial Day recess. For a copy of H.R. 1890, the House version of the RIA (introduced by a majority of the House Ways and Means Committee) click HERE.

Closely Held REITs

All revenue raising provisions contained in the Senate version of the legislation, including a provision that would have disqualified certain "closely-held REITs," were dropped from the final legislation. This provision would have modified the "widely held" ownership test that REITS must pass by prohibiting any "person" (other than another REIT, a pension plan or certain other entities) from owning 50% or more of the vote or value of a REIT's stock.

Tenant Improvements

Also under the legislation, real estate companies like REITs will be able to expense 50% of their second-generation tenant improvements in 2003 and 2004 (up from the 30% under prior law).

More Information

For further background on the Jobs and Growth Reconciliation Tax Act of 2003, click HERE.

If you have any questions about these issues, please contact
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