

JO Knows How Carried Interests Affect Real Estate

DECEMBER 20, 2022 | BY: THE REAL ESTATE TEAM

Back in [March of 2022](#) we wrote to you about the changes to the carried interest rules but there could be another related change on the horizon. Last week, Senate Democrats announced a new piece of legislation called the Inflation Reduction Act of 2022. This is a 700+ page piece of legislation that is a net revenue raiser intended to decrease the deficit. The spending that this bill includes to fight climate change and extend the Affordable Care Act is paid for with a 15% corporate minimum tax, prescription drug pricing reform, IRS Tax enforcement and the modification of the so-called carried interest loophole.

What Has Changed Under the Proposed Legislation

- The holding period required to receive long term capital gain treatment is changed from three to five years.
- There are two exceptions to the five-year holding period, which would revert to the three-year holding period:
 - Taxpayers with adjusted gross income of less than \$400,000
 - Gains attributable to a real property trade or business (Section 1231 gain)
- The holding period start date is after the latest of:
 - The date on which the taxpayer acquired substantially all of the applicable partnership interest with respect to which the amount is realized
 - The date on which the partnership in which such applicable partnership interest is held acquired substantially all of the assets held by such partnership

What Does This Mean?

This new legislation has expanded the applicability of Section 1061 (carried interest) to the sale of real estate who had previously been excluded. This means that those individuals that receive a carried interest will need to watch the holding period much more closely in order to include the gain on the sale of the underlying real estate as long term capital gains.

Next Steps

This is only proposed legislation and still needs to go through the House and Senate and could be further changed through the process. The Democrats will need to be united in order to get this bill passed. Which pieces of this bill remain intact and which ones change or are removed remains to be seen. The carried interest change makes up only \$14B of the \$739B in revenue raisers included in the bill so it's a rather small portion of the overall impact but greatly affects the real estate industry. We will continue to watch for changes to the proposed legislation and report back as needed. Feel free to reach out to us with questions or concerns as we are here to help you achieve your goals while minimizing the tax impact. To learn more about Johnson O'Connor's Real Estate services, click [here](#).

RELATED INDUSTRIES

Real Estate