

1031 Exchanges in Biden's Administration

What is Known and What is Unknown



The Known

On January 20, 2021, Democratic President Joe Biden will lead the Executive Branch of government, and Democrats will have a majority in both houses of Congress. More specifically, following the Georgia runoff election in which Raphael Warnock (D) and Jon Ossoff (D) won the two open U.S. Senate seats, the Senate will consist of 50 Republicans and 50 Democrats. If every Senator votes along party lines, there will be a tie and Vice President Kamala Harris will make the tie-breaking vote, giving the Democrats the majority.

With this majority, Democrats in the Senate will likely look to the Budget Reconciliation process to move tax legislation forward. Budget Reconciliation is an expedited process that prevents a filibuster and requires only a majority vote to pass legislation, compared to the 60 votes needed for other Senate measures. However, the Reconciliation process is strictly limited to spending, debt limits, and certain tax issues, within a well-defined procedural network. Under Reconciliation, changes can be made to spending, revenue, tax laws, or debt levels so they are consistent with the adopted Budget Resolution. There are many elements and limitations involved in Reconciliation. For example, the Reconciliation cannot increase the deficit beyond the budget window, unless other provisions in the Reconciliation fully offset any new costs.

The Unknown

No one can be certain about the order of the Biden administration's priorities; however, containment of COVID-19, including increased vaccinations and availability of personal protective equipment, will likely be at the top of the list. Until COVID-19 is under control, it will be difficult for the administration and Congress to address the economy and job growth. It is likely additional economic stimulus will be needed to help combat the impact of COVID-19 on the national economy. Once the spread of COVID-19 has been brought under control, the Biden administration and Congress may pursue tax increases for corporations and individuals, among other things.

During the campaign, Biden's camp proposed a number of tax increases that include increasing the corporate tax rate to 28%, unwinding the Tax Cuts & Job Act's lower rates on individuals, increasing capital gain tax rates for higher earners, and other proposals that would result in nearly \$4 billion in new taxes. One aspect of the Biden campaign's tax plan included a proposal to modify or eliminate Internal Revenue Code Section 1031 tax-deferred exchanges. Real estate investors, farmers, ranchers, Real Estate

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Investment Trusts (REITs), real estate professionals, and many other ancillary industries have been concerned about a possible attempt to modify or eliminate the 100-year-old tax code provision, Section 1031. As we emerge from the pandemic, many tax and real estate professionals believe 1031 tax-deferred exchanges will be essential in revitalizing the economy, particularly as buildings are repurposed and as capital is invested into real estate assets that need to be improved or redeveloped.

In general, campaign tax proposals provide a broad backdrop of a President's intended tax priorities. Once that person is elected, the process of modifying tax laws begins in the House's Ways and Means Committee and in the Senate's Finance Committee. As these two committees work through the process of changing tax laws and writing a final tax bill, they often incorporate some, but not all, of the broad campaign tax proposals. Final tax bills approved by the House and Senate are generally less comprehensive than the proposals made while campaigning.

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